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IN THE

SUPREME COURT

OF THE

UNITED STATES

OCTOBER TERM, 1935

NORTHERN PACIFIC RAILWAY COMPANY, a Corporation, *Appellant*, vs. STATE OF WASHINGTON, *Appellee.*	No. 529
GREAT NORTHERN RAILWAY COMPANY, a Corporation, *Appellant*, vs. STATE OF WASHINGTON, *Appellee*,	No. 573
THE PACIFIC TELEPHONE AND TELEGRAPH COMPANY, a Corporation, *Appellant*, vs. THE TAX COMMISSION OF THE STATE OF WASHINGTON and T. S. HEDGES and T. M. JENNER, as Members of the Tax Commission of the State of Washington, *Appellees.*	No. 544

APPEALS FROM THE SUPREME COURT OF THE STATE OF WASHINGTON

BRIEF OF APPELLEES

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STATE PRINTING PLANT

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BRIEF OF APPELLEES

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Assistant Attorney General of the State of Washington,

Attorneys for Appellees.

STATEMENT

These appeals having been assigned for argument on the same day, and substantially all of the legal questions involved being common to all, the appellees, to avoid needless repetition, have interposed but one brief in the three appeals.

Abbreviations:

For convenience and brevity, the appellant, Northern Pacific Railway Company, will be herein referred to as the "N. P.;" the appellant, Great Northern Railway Company, as the "G. N.;" the appellant, Pacific Telephone & Telegraph Company, as the "P. T.;" the tax commission of the state of Washington, as the "tax commission;" the state of Washington, as the "State;" the Interstate Commerce Commission, as the "I. C. C.;" and the Department of Public Works of the State of Washington, as the "D. P. W."

Unless otherwise qualified, the word "intrastate" means the traffic or business of the particular appellant, both beginning and ending in the state of Washington.

The N. P. and G. N. Cases:

These are appeals from judgments of the State supreme court reversing judgments for defendant in separate actions brought by the State in the superior court for Thurston county, Washington, against these companies to recover the occupational tax measured by 1½% of the intrastate gross income imposed on steam railroads by Chapter 191, Laws of Washington of 1933, for the last five months of 1933. The N. P. is a Wisconsin corpora-

tion, and the G. N., a Minnesota corporation, each owning and operating lines of steam railway in Washington and other states.

The complaint in each case alleges non-payment of the tax, and prays judgment for the amount. (NP Rec. 1-6; GN Rec. 1-6.)

The answers while admitting the amount of the disputed tax to be substantially as alleged by the State, and that the same is unpaid, deny liability therefor on the grounds:

(1) That under the State laws and constitution the defendant is not allowed to withdraw from its local business while continuing to carry on its interstate business;

(2) That it conducted its intrastate business at a loss in 1932 and 1933; and

(3) That its intra and interstate traffic is hauled over the same rails, in the same trains, and by the same employes, and is inseparably commingled and mutually dependent, and that abandonment of its local business, even if possible, would result in the loss of its local revenues with no considerable reduction in its expenses, and would require an increase in interstate tariffs higher than the traffic would bear. (NP Rec. 7-13; GN Rec. 7-20.)

The State replied, denying the material allegations of the railroads' answers, and alleging affirmatively (1) that defendant had never applied to the D. P. W. for permission to increase its tariffs by reason of the occupational tax; and (2) that as a result of the adoption in 1932 and 1933 by the people and state legislature of the

New Tax Plan including the 40-mill limit act and occupational tax act, the tax burden of defendants and other railroads had been greatly reduced as compared with the *ad valorem* taxes which would have been collectible from said companies under the old tax plan. (NP Rec. 17-32; GN Rec. 29-44.)

The cases were tried by the court without a jury resulting in each case in a judgment for defendant (NP Rec. 54; GN Rec. 77-8), from which judgments, appeals were taken to the State supreme court (NP Rec. 252; GN Rec. 253), where, in each case, the judgment was reversed with directions to the lower court to enter judgment for the State for the amount of the tax. (NP Rec. 67; GN Rec. 97.) Each company has appealed to this court.

The P. T. Case:

This is an appeal from the judgment of the state supreme court reversing a decree in an injunction suit instituted by the P. T., a California corporation, in the superior court for Thurston county, Washington, permanently enjoining the defendant, tax commissioners, from enforcing as against the P. T. the provisions of said chapter 191, Laws of 1933, in so far as it imposes an occupational tax on the P. T., an interstate telephone and telegraph company, equal to 3% of its intrastate gross receipts. (Ab. 4, 13.)

In its amended complaint, the P. T. assails the tax on substantially the same grounds urged by the railroad companies, save that it does not allege that it is losing money on its intrastate business, but alleges, on the contrary, that it is earning a return of at least 1.75%

on the fair value of its operating property. (PT Rec. 4.)

The defendant, tax commissioners, answered putting in issue the material allegations of the amended complaint, and setting up as an affirmative defense that the P. T. had never applied either to the D. P. W. or to any other state department for permission either to renounce its intrastate business, or to increase its tariffs because of the offending occupational tax. (PT Rec. 13.) These defenses stand admitted since no reply was interposed thereto. (Rem. Comp. Stat., Sec. 297.)

The trial resulted in a decree permanently enjoining the defendant tax commissioners from enforcing the provisions of said Occupational Tax Act of 1933 as against the P. T. (PT Rec. 15-17.) From such decree, such commissioners appealed to the state supreme court, which reversed the decree of the lower court with instructions to dismiss the suit. The P. T. has appealed to this Court.

THE 1933 STATE OCCUPATIONAL TAX ACT:

By the law here assailed, an occupational tax is imposed for the two-year period ending July 31, 1935, upon those engaged in various business activities in the state, measured by the gross proceeds derived from mining, manufacturing, wholesaling or jobbing, retail distributing, and performing of services. The rates imposed vary with the different activities. Thus, on the gross income of stock brokers, the rate is 2%; on steam railways and highway transportation companies, 1½%; and on light and power companies, water companies and telephone and telegraph companies, 3%. (Laws 1933, Ch. 191, Sec. 2, pp. 870-5.)

The tax is imposed on municipal corporations operating utilities and conducting businesses, the same as upon private enterprises (Sec. 2-e), and has been sustained as such. See *Tacoma v. State Tax Commission*, 177 Wash. 604.

Other states imposing similar excises are shown in the footnote.*

It is conceded, as above noted, that as to interstate public service companies the tax commission construes the Act as not applying to the gross income from interstate business, but to the gross income from intrastate business only.

The tax has been repeatedly sustained by the State supreme court as against attacks made on its constitutionality by various classes of taxpayers. See *State ex rel. Stiner v. Yelle*, 174 Wash. 402; *Cascade Tel. Co. v. State Tax Commission*, 176 Wash. 616; *Tacoma v. State Tax Commission*, 177 Wash. 604; *Supply Laundry Co. v. Jenner*, 178 Wash. 72; *State v. N. P. Ry. Co.*, 83 Wash. Dec. 52, 48 Pac. (2d) 931, NP Rec. 54.

Indeed, the tax was sustained by a three-judge federal district court, in an attack on its constitutionality by five interstate railroads including the two railroad appellants here, made upon the same grounds as urged on these appeals. See *Chicago, M., St. P. & P.*

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*Arizona: ch. 77, Laws 1935; Indiana: ch. 50, Acts, 1933; Kentucky: ch. 25, Laws 1934; Mississippi: ch. 119, Laws 1934; New Mexico: ch. 78, Laws 1935; New York City: Local Law No. 21, 1934, amended by Local Law No. 2, 1935; North Dakota: ch. 276, Laws 1935; Oklahoma: Laws 1935, p. 131, ch. 88, art. 6; Ohio: Laws 1933-4, Pt. 2, p. 821; West Virginia: ch. 38, p. 219, Ex. Sess. 1933.

R. Co. v. Hedges, 5 Fed. Supp. 752, to which we will later refer.

The State supreme court has heretofore sustained excise taxes similar to the 1933 Occupational Tax Act as applied to interstate public service companies. *State v. Northern Express Co.,* 80 Wash. 309; *Pacific Tel. & Tel. Co. v. Seattle,* 172 Wash. 649 (affirmed: 291 U. S. 300); *Puget Sound P. & L. Co. v. Seattle,* 172 Wash. 668 (affirmed: 291 U. S. 619). And see: *Spokane International R. Co. v. State,* 162 Wash. 395.

UNITED STATES SUPREME COURT DECISIONS SUSTAINING EXCISE TAXES EXACTED OF INTERSTATE PUBLIC SERVICE COMPANIES.

Express Companies:

In *Osborne v. Mobile,* 16 Wall. 479, the court upheld a city ordinance fixing the annual license fees for express companies doing business within its limits as follows: if doing an interstate business, $500; if doing intrastate business only, $100; and if doing intra-city business only, $50. The attack was made by a corporation doing an interstate business.

This case, however, was later disapproved in *Leloup v. Port of Mobile,* 127 U. S. 640, 645, as not in harmony with the court's later decisions.

In *Pacific Express Co. v. Seibert,* 142 U. S. 339, a state statute imposing a privilege tax of 2% of the company's intrastate gross receipts in addition to the *ad valorem* tax paid on the company's tangible property, and providing for a penalty of $100 a day for delinquency in making its report and paying the tax, and prohibiting the company from carrying on intrastate business while such tax was delinquent, was upheld as not violative of the commerce clause.

Osborne v. Florida, 164 U. S. 650, involved the validity of an occupation or license tax imposed by cities upon those pursuing divers occupations and professions, in so far as it affected express companies who were required to pay a tax of from $10 to $200 a year depending on the size of the city. As to express companies the state court had construed the act as applying only to intrastate and not to interstate business. As so construed, the supreme court held the act not violative of the federal constitution. In so holding, the court said:

"It has never been held, however, that when the business of the company which is wholly within the State, is but a mere incident to its interstate business, such fact would furnish any obstacle to the valid taxation by the State of the business of the company which is entirely local. So long as the regulation as to the license or taxation does not refer to and is not imposed upon the business of the company which is interstate, there is no interference with that commerce by the state statute. * * * The statute herein differs from the cases where statutes upon this subject have been held void, because in those cases the statutes prohibited the doing of any business in the state whatever unless upon the payment of the fee or tax. It was said as to those cases that as the law made the payment of the fee or the obtaining of the license a condition to the right to do any business whatever, whether interstate or purely local, it was on that account a regulation of interstate commerce, and therefore void. Here, however, under the construction as given by the state court, the company suffers no harm from the provisions of the statute. It can conduct its interstate business without paying the slightest heed to the act, because it does not apply to or in any degree affect the company in regard to that portion of its business which it has the right to conduct without regulation from the State." (P. 655.)

Sleeping Car Companies;

By the Mississippi Code of 1892, a tax was imposed "on each sleeping and palace car company carrying

passengers from one point to another within the state, one hundred dollars, and twenty-five cents per mile for each mile of railroad track (in the state) over which the company runs its cars." The state constitution declared sleeping car companies to be common carriers. In *Pullman Co. v. Adams,* 189 U. S. 420, the supreme court, following its former decision of *Osborne v. Florida, supra,* held the tax valid.

Again, in *Allen v. Pullman Co.,* 191 U. S. 171, it was held that a tax law of Tennessee requiring sleeping car companies to pay a tax of $3,000 per annum in lieu of all other except *ad valorem* taxes for one or more passengers taken up at one point within the state and delivered at another and transported wholly within the state and which did not refer to or affect the interstate business of the companies, would not be regarded as disguised attempt to tax the privilege of engaging in interstate commerce, where under the laws of the taxing state, it was not compulsory for a corporation engaged in interstate commerce to carry on that part of its business which was wholly within the state, and was therefore not repugnant to the commerce clause of the federal constitution. In so holding the court followed its former rulings in *Osborne v. Florida, supra,* and *Pullman Co. v. Adams, supra.*

Telegraph Companies:

In *Postal Tel.-Cable Co. v. Fremont,* 255 U. S. 124, it was held that a license tax of $60 a year imposed by a city on a telegraph company for the privilege of doing intrastate business, could not be declared an unconstitutional burden on its interstate business merely because the local business was unprofitable, where the tax ordi-

nance was in force when the company entered the place and the tax was paid without objection for a series of years, the circumstances thus repelling any intent to invade interstate commerce in levying it, and where the state law afforded means to prevent the tax from burdening the interstate business through an application to increase intrastate rates, of which the company had not sought to avail itself.

And in *Postal Tel.-Cable Co. v. Richmond*, 249 U. S. 252, a license tax imposed on intrastate business was upheld as against the objection that it imposed a burden on the company's interstate business because the net receipts from its intrastate business were insufficient to pay the tax, and the payment would therefore have to be made from interstate receipts.

In *Western Union Tel. Co. v. Alabama*, 132 U. S. 472, it appeared that a statute of Alabama imposed a tax "on the gross amount of the receipts by any and every telegraph company derived from the business done by it in this state." The company reported to the board of assessors only its gross receipts received from business wholly transacted within the state. The board required a further return by the company of gross receipts from messages carried partly within and partly without the state. The company made such further return, and the tax was imposed on the gross receipts as shown by the two returns. In holding that the tax imposed on the messages comprised in the second return was unconstitutional, the court said:

"The principle is, in regard to telegraph companies which have accepted the provisions of the Act of Congress of July 24, 1866 (Rev. Stat. Sec. 5263 to Sec. 5268), that they shall not be taxed by the authorities of a state

for any messages, or receipts arising from messages, from points within the state to points without, or from points without the state to points within, but that such taxes may be levied upon all messages carried and delivered exclusively within the state. The foundation of this principle is that messages of the former class are elements of commerce between the states and not subject to legislative control of the states, while the latter class are elements of internal commerce solely within the limits and jurisdiction of the state, and, therefore, subject to its taxing power." (p. 473.)

In *Telegraph Company v. Texas*, 105 U. S. 460, it was held that state laws, so far as they impose upon telegraph companies a specific tax on each message transmitted beyond the state, are unconstitutional; but it was said that "any tax which the state may put on messages by private parties, and not by agents of the United States, from one place to another exclusively within its own jurisdiction, will not be repugnant to the Constitution of the United States."

In *Postal Tel.-Cable Co. v. Charleston*, 153 U. S. 692, it was held that a city ordinance imposing a license tax of $500 upon a telegraph company upon business done exclusively within the city was a valid exercise of the police power and was not an interference with interstate commerce.

In *Ratterman v. Western Union Tel. Co.*, 127 U. S. 411, the court, after an exhaustive review of its earlier decisions, held that a single tax of 5% of the gross receipts assessed under an Ohio law upon receipts of a telegraph company derived partly from interstate, and partly from intrastate commerce, but which were capable of separation, was invalid in proportion to the extent such receipts were derived from interstate commerce, but was otherwise valid.

In *Williams v. Talladega,* 226 U. S. 404, it was held that a municipal license tax on an interstate telegraph company's right to do local business within the state could not be deemed an unconstitutional burden on interstate business because a test for eleven months showed that the company did its intrastate business at that point at a net loss of 86 cents. The tax measure, however, was adjudged invalid because of not excepting from its application messages transmitted for the federal government.

Telephone Companies:

New Jersey Bell Tel. Co. v. State Board, 280 U. S. 338, involved the validity of an occupational tax measured by the state's proportion of the company's entire gross receipts, both intra and interstate. *The company paid without protest the tax based on local receipts.* The court condemned the tax in so far as measured by interstate receipts, Justices Holmes and Brandeis, however, dissenting.

The supreme court's most recent expression on the right of a state to impose an occupational or business tax on public service companies doing both an intra and interstate business, is found in *Cooney v. Mountain States Tel. & Tel. Co.,* —— U. S. ——, 79 L. ed. 498, 55 Sup. Crt. 477, where the court refused to sustain an excise tax imposed on an interstate telephone company and measured by a certain imposition on each telephone instrument used in its business, varying from 20 cents to $2 per year, depending on the number of phones and the rates charged. The offending state law provided that every corporation "engaged in the business of operating or maintaining telephone lines and furnishing telephone service in the State of Montana * * * shall pay

* * * a license tax * * * for each telephone instrument used, controlled and operated by it in the conduct of such business." The court held that by this language the tax was clearly intended to be imposed on telephone instruments used not only in intrastate but in interstate business and was therefore void.

In considering the following excerpt from the opinion (79 L. ed. 502), the Court will bear in mind that there the tax was on an instrumentality used by the company in carrying on both its intra and interstate activities, while here the tax is measured by intrastate gross income only:

"The business is the maintaining of telephone lines and the furnishing of telephone service in the state. No distinction is made between interstate and intrastate service. The tax is then stated to be 'for each telephone instrument used, controlled and operated.' Again, there is no limitation as to use, control or operation in intrastate business. The tax is 'based upon the number of telephone instruments owned, controlled and operated' during all or any part of the calendar year. A 'telephone instrument' is defined in section two of the act as 'a transmitter and receiver capable of use in the transmitting and receiving of telephone communications.' The tax is thus laid simply by reason of the fact that the company is furnishing telephone service and is based upon the number of telephone instruments used in that service without regard to its character whether intrastate or interstate. * * * All the telephone instruments, not excepted, whether they are used in intrastate or interstate commerce and however the service is paid for, are left subject to the tax. * * * But the tax is not laid on revenues. It is not laid on revenue derived from monthly rates as distinguished from toll charges. It is not imposed with respect either to the nature of the revenue, or to the character of the service from which the revenue is derived, or to the manner in which the charges for the service are fixed.

"The evidence supports the finding that these tele-

phone instruments are available for interstate and foreign communications. * * * It appears that in the operation of this unified system, the telephone instruments are the means by which the customers command at their pleasure the service they desire whether intrastate or interstate. And, so far as the instruments are not excepted, the tax is laid indiscriminately with respect to each of these facilities, regardless of the nature of their use.

"There is no question that the State may require payment of an occupation tax from one engaged in both intrastate and interstate commerce." (Italics ours.)

In a footnote the court here cites a large number of authorities including all those heretofore reviewed, and then continues:

"But a state cannot tax interstate commerce; it cannot lay a tax upon the business which constitutes such commerce or the privilege of engaging in it. And the fact that a portion of a business is intrastate and therefore taxable does not justify a tax either upon the interstate business or upon the whole business without discrimination. *Leloup v. Mobile*, 127 U. S. 640, 32 L. ed. 311, 8 S. Ct. 1380, 2 Inters. Com. Rep. 134. *There are 'sufficient modes' in which the local business may be taxed without the imposition of a tax 'which covers the entire operations.'* Id., p. 647. See *Williams v. Talladega*, 226 U. S. 404, 419, 57 L. ed. 275, 281, 33 S. Ct. 116." (Italics ours.)

In using the last expression quoted, the court unquestionably had in mind the imposition of a tax measured by intrastate revenues—excises which, as heretofore shown, it had so often theretofore sustained.

Railroad Companies:

Reading R. Co. v. Pennsylvania, 15 Wall. 232, involved the validity of a Pennsylvania statute imposing a tax of two to five cents on every ton of freight transported by any railroad or canal in that state. The tax was held valid as to commerce wholly within the state, but void as to freight hauled in interstate commerce. As

to the tax imposed on intrastate freight, the court said (p. 282):

"But while holding this, we recognize fully the power of each state to tax at its discretion its own internal commerce, and the franchises, property or business of its own corporations, so that interstate intercourse, trade, or commerce, be not embarrassed or restricted. That must remain free."

But in *Reading R. Co. v. Pennsylvania*, 15 Wall. 284, a state statute imposing an excise tax of three fourths of 1% on both the intra and interstate gross receipts of domestic railroad corporations, was upheld as not violative of the commerce clause of the constitution, three justices dissenting.

And in *State of Maine v. Grand Trunk Ry. Co.*, 142 U. S. 217, the court sustained as to a foreign corporation, and as not violative of the commerce clause, a state statute requiring every railroad corporation operating in the state to pay "an annual excise tax for the privilege of exercising its franchise," the amount of the tax being determined according to a sliding scale proportioned to the average gross earnings per mile within the state for the preceding year. Four justices dissented.

In *Lehigh Valley R. Co. v. Pennsylvania*, 145 U. S. 192, it was held that a state gross receipts tax of 8/10ths of 1% against a domestic railroad corporation on account of transportation between points in the same state, but passing, during transportation, without the state, was not a tax upon interstate commerce, and did not infringe the provisions of the federal constitution. The court said:

"Taxation is undoubtedly one of the forms of regulation, but the power of each state to tax its own internal commerce, and the franchise, property or business of its

own corporations engaged in such commerce, has always been recognized, and the particular mode of taxation in this instance is conceded to be in itself not open to objection. And while interstate commerce cannot be regulated by a state by the laying of taxes thereon, in any form, yet when the subjects of taxation can be separated so that that which arises from interstate commerce can be distinguished from that which arises from commerce wholly within the state, the distinction will be acted upon by the courts, and the state permitted to collect that arising upon commerce solely within its own territory. *Ratterman v. West. Union Tel. Co.*, 127 U. S. 411, 424."

But in the later case of *Galveston, Harrisburg, etc. Ry. Co. v. Texas*, 210 U. S. 217, the court held, in a five-to-four decision that a Texas statute imposing a tax upon domestic railroad companies equal to 1% of their gross receipts was, as to those companies whose revenue included receipts from interstate business, a burden on interstate commerce and, as such, violative of the commerce clause of the federal constitution, thus, to the extent that interstate receipts were taxed, reversing by a bare majority, its earlier decisions in this regard.

Never, however, has this court in even a minority opinion questioned the right of the states to impose an excise tax on the intrastate gross receipts of either domestic or foreign public service corporations, doing both intra and interstate business, whatever the character of the service rendered.

In *St. Louis Southwestern Ry. Co. v. Arkansas ex rel. Norwood*, 235 U. S. 350, it was held that the annual franchise tax imposed by an Arkansas statute upon a railroad corporation "for the privilege of exercising its franchise in this state" of a specified percentage of the corporation's outstanding capital stock represented by

property owned and used in business transacted in the state was not repugnant to the commerce clause of the federal constitution, as applied to a foreign railway company doing both interstate and intrastate business, where, as construed by the state court, such tax was upon the right to exercise the privilege to transact intrastate business in corporate form, the amount of the tax being fixed solely by reference to the property of the corporation that was within the state and used in business transacted within the state, excluding any imposition upon, or interference with, interstate commerce.

In *People ex rel. Cornell Steamboat Co. v. Sahmer*, 235 U. S. 549, the court held a state excise tax or license fee equal to 5/10th of 1% upon intrastate gross earnings imposed on transportation and transmission corporations and associations for the privilege of doing business in the state in corporate form not to be an invalid regulation of commerce as applied to a navigation company engaged in the business of towing upon the Hudson river.

We come now to the outstanding case of *Ohio River & W. R. Co. v. Dittey*, 232 U. S. 576,—the *"Ohio Tax Cases."* By an act of 1911, the Ohio legislature prescribed various taxes, some upon property and others upon franchises and privileges with sundry provisions, penal and otherwise, for their collection. The tax there in question was limited in its operation to certain public utilities, including railroads. Each railroad doing business in the state was required to pay an excise tax of 4% of its entire gross earnings from business done

within the state except business done for the federal government.

In sustaining such tax as to railroads, the court held among other things:

That the tax was not void as confiscatory or violative of the due process clause because the complaining roads were not earning a fair return from their local business on the value of their operating property, devoted thereto, and one of which roads was operating at a loss;

That such roads were not arbitrarily discriminated against, contrary to the equal protections clause, because the tax was not exacted of all public utilities, or because the public utilities included, were not all taxed at the same rate; and

That the tax was not void for lack of uniformity because imposed in addition to an ad valorem tax, as being double taxation.

Counsel for the various appellants waive aside the *Ohio Tax Cases, supra,* with the statement that there "the tax was for the privilege of exercising the corporate franchise granted by the state to a domestic corporation," and liken it to *Kansas etc. R. Co. v. Bodkin,* 240 U. S. 227. (NP Brief, p. 33.)

True, in the *Bodkin* case the tax sustained was "on the primary corporate franchise granted by the State" (240 U. S. 232), but this was not true of the *Ohio Tax Cases.* In the latter case the imposition was stated in the statute to be "in the nature of an excise tax, for the privilege of carrying on its intrastate business," and *was imposed equally and alike on corporations, part-*

nerships, and individuals. (232 U. S. 580.) Indeed, appellants' counsel there conceded that the offending tax was not "upon corporate franchises or privileges, as such." (232 U. S. 581.) And in its opinion the court speaks of the tax as one "with respect to the privilege or *occupation.*" (232 U. S. 594.)

The fact that in the *Ohio Tax Cases, supra,* the objecting taxpayers were domestic corporations does not detract from the controlling force of the decision. *Galveston, etc. Ry. Co. v. Texas,* 210 U. S. 217, 228; *Southern Ry. Co. v. Greene,* 216 U. S. 400, 417-8; *Chicago, M., St. P. & P. R. Co. v. Hedges,* 5 Fed. Supp. 752, 760.

In the case last cited Judge Cushman, after reviewing the *Ohio Tax Cases,* said with respect to counsel's attempted distinction:

"There is no reason for contending that the interstate commerce carriage by a domestic corporation can be burdened as the result of a state law, and that carried by foreign corporations cannot. Northern Securities Co. v. United States, 193 U. S. 197."

INTERSTATE COMMERCE NOT UNLAWFULLY BURDENED, WHERE APPELLANTS' TOTAL TAX, PROPERTY AND EXCISE, NOT GREATER THAN MIGHT BE LAWFULLY IMPOSED ON AN AD VALOREM BASIS ALONE.

In this connection, we quote the following from the decision of the state supreme court (*State v. N. P. Ry. Co.,* 83 Wash. Dec. 52, 59-61, 48 Pac. (2d) 931, 935; NP Rec. 61-2):

"It must be remembered that chapter 191 of the Laws of 1933 applies to every person engaging or continuing in business within this state, with a comparatively few exceptions. The law may be said to be a general one and applies to all businesses within the state. In this respect, it is somewhat analgous to a property tax which all persons, with comparatively few exceptions provided for in the statute, are required to pay upon

the property owned by them. The state has the authority to tax property which is used in interstate commerce and which is regularly and permanently located within its limits, where the ascertainment of the amount assessed is dependent upon the value of the property within the state, as the property of other citizens is taxed. *Leloup v. Port of Mobile*, 127 U. S. 640, 8 S. Ct. 1380; *Western Union Telegraph Co. v. Kansas*, 216 U. S. 1, 30 S. Ct. 190.

"Even though the respondent in this case cannot retire from its intrastate business without also retiring from its interstate business, we think that the excise tax imposed upon the gross income from the intrastate business is not such a direct burden upon interstate commerce as to require that the tax be held void.

"Attention at this point should be called to chapter 4 of the Laws of 1933, p. 47, Rem. 1933 Sup. § 11238-1 [P. C. § 6882-77a], which was initiative measure 64, and generally referred to as the '40-mill tax limit for taxation' law. In that act, it was provided that the aggregate of all taxes upon real and personal property in the state should not exceed in any one year forty mills on the dollar of assessment valuation, which should be based upon fifty per cent of the true and fair value of the property in money, with some exceptions which are not here material. The respondent, by reason of this law, has been relieved from paying a very large sum of money as taxes upon the property which it owns in this state and which was subject to taxation, even though devoted to interstate commerce. It is a matter of common knowledge that, under the 40-mill tax limit law, property is now paying about half of what it paid for general taxes prior to the passage of that law; in other words, that, by reason of the law limiting the amount to forty mills, the tax burden upon both real and personal property of the state has been reduced approximately one-half. Having thus provided for a reduction of taxes upon real and personal property, it was necessary for the legislature to find other sources of revenue, and chapter 191 was undoubtedly passed for this reason.

"So far as we are informed, the Federal supreme court has at no time distinctly held that an excise tax, such as that of this state, which is imposed upon all businesses, is such a direct burden upon interstate com-

merce as to render the act of the legislature unconstitutional."

In amplification of what was said by the State supreme court in this connection, may we here set forth the appellees' position in the court below. It was contended: (1) that the State's revenue laws must be considered collectively to determine whether the tax complained of unlawfully burdens appellants' interstate business; (2) that were appellants' physical properties and franchises taxed as in 1932 and prior years to cover the entire cost of state government, such tax could not be deemed an unlawful burden on appellants' interstate business; and (3) that the undisputed evidence shows that under the present state revenue laws, each appellant railroad's entire tax burden is materially less than its *ad valorem* taxes alone would have been, were the State's necessary revenues raised by property taxation alone.

DETERMINATION OF METHOD OF DISTRIBUTING TAX BURDEN IS LEFT TO THE STATES.

This was thus recognized in *Lawrence v. State Tax Commission*, 286 U. S. 276, 279-280, where Your Honors said in sustaining, as not violative of the due process clause, a Mississippi law imposing a tax on the net income of its residents derived wholly from activities carried on by them outside of the state:

"The obligation of one domiciled within a state to pay taxes there, arises from unilateral action of the state government in the exercise of the most plenary of sovereign powers, that to raise revenue to defray the expenses of government and to distribute its burdens equably among those who enjoy its benefits. Hence, domicile in itself establishes a basis for taxation. Enjoyment of the privileges of residence within the state, and the attendant right to invoke the protection of its law, are inseparable from the responsibility for sharing the costs of government. See *Fidelity & Columbia Trust*

Co. v. Louisville, 245 U. S. 54, 58; *Maguire v. Trefry,* 253 U. S. 12, 14, 17; *Kirtland v. Hotchkiss,* 100 U. S. 491, 498; *Shaffer v. Carter,* 252 U. S. 37, 50. The Federal Constitution imposes on the states no particular modes of taxation, and apart from the specific grant to the federal government of the exclusive power to levy certain limited classes of taxes and to regulate interstate and foreign commerce, it leaves the states unrestricted in their power to tax those domiciled within them, so long as the tax imposed is upon property within the state or on privileges enjoyed there, and is not so palpably arbitrary or unreasonable as to infringe the Fourteenth Amendment. * * *

"It is enough, so far as the constitutional power of the state to levy it is concerned, that the tax is imposed by Mississippi on its own citizens with reference to the receipt and enjoyment of income derived from the conduct of business, regardless of the place where it is carried on. The tax, which is apportioned to the ability of the taxpayer to bear it, is founded upon the protection afforded to the recipient of the income by the state, in his person, in his right to receive the income, and in his enjoyment of it when received. These are rights and privileges incident to his domicile in the state and to them the economic interest realized by the receipt of income or represented by the power to control it, bears a direct legal relationship."

STATE REVENUE LAWS MUST BE EXAMINED COLLECTIVELY TO DISCOVER WHETHER APPELLANTS' INTERSTATE BUSINESS IS UNLAWFULLY BURDENED BY TAXES IMPOSED.

In *Baker v. Druesedow,* 263 U. S. 137, 142, the court said:

"Where illegal discrimination was practiced, it is immaterial whether it was effected by a single assessing board or through the action of two independent boards. *Greene v. Louisville & Interurban R. R. Co.,* 244 U. S. 499, 513; *Southern Ry. Co. v. Watts,* 260 U. S. 519, 526."

The converse, we submit, must be true. If the operation of the state's revenue statutes as an entirety do not result in an invasion of any of appellants' constitu-

tional rights or burden their interstate commerce, appellants cannot be heard to complain.

The principle is thus clearly announced in *Gregg Dyeing Co. v. Query*, 286 U. S. 472, 479-80:

"The state court answered the contention as to discrimination against interstate commerce by referring to other statutes of the state imposing a tax upon the sale and use of gasoline within the state. The state court said that the act in question 'taxes all gasoline stored for use and consumption upon which a like tax has not been paid under other statutes. By the kindred acts all users are taxed.' But appellants question the right to invoke other statutes to support the validity of the act assailed. To stand the test of constitutionality, they say, the act must be constitutional 'within its four corners,' that is, considered by itself. This argument is without merit. The question of constitutional validity is not to be determined by artificial standards. What is required is that state action, whether through one agency or another, or through one enactment or more than one, shall be consistent with the restrictions of the Federal Constitution. There is no demand in that constitution that the state shall put its requirements in any one statute. It may distribute them as it sees fit, if the result, taken in its totality, is within the state's constitutional power. When the Supreme Court of the state has held that two or more statutes must be taken together, we accept that conclusion as if written into the statutes themselves. *Hebert v. Louisiana*, 272 U. S. 312, 317. See *Lindsley v. National Carbonic Gas Co.*, 220 U. S. 61, 73."

True, a State can neither tax the act of engaging in interstate commerce nor lay a tax on the gross receipts therefrom. (*Pullman Co. v. Richardson*, 261 U. S. 330, 338.)

But on the other hand, it has been held by this Court many times that an apportionment of the cost of State government to an interstate utility company according to the relative value of the property of such company

permanently located or commonly used by it within the state in such interstate commerce is not violative of the commerce clause. (*Cudahy Packing Co. v. Minnesota,* 246 U. S. 450, 453; *Wells, Fargo & Co. v. Nevada,* 248 U. S. 165, 167; *Union Tank Line Co. v. Wright,* 249 U. S. 275, 282; *Pullman Co. v. Richardson,* 261 U. S. 330, 338.)

It has also been frequently held that an apportionment of the expense of state government to an interstate utility company according to its net income including that earned in its interstate activities does not violate the commerce clause. (*United States Glue Co. v. Oak Creek,* 247 U. S. 321; *Shaffer v. Carter,* 252 U. S. 37, 57; *Underwood Typewriter Co. v. Chamberlain,* 254 U. S. 113; *Atlantic Coast Line v. Daughton,* 262 U. S. 413, 416.)

And the rule is likewise established by this court that a tax measured by an interstate utility company's gross income including a mileage proportion of that earned in interstate commerce imposed in lieu of property taxes, will be sustained as not violative of the commerce clause, if such exaction does not exceed that which could lawfully have been imposed on an *ad valorem* property tax basis. *U. S. Express Co. v. Minnesota,* 223 U. S. 335; *Cudahy Packing Co. v. Minnesota,* 246 U. S. 450; *Pullman Co. v. Richardson,* 261 U. S. 330.

In *U. S. Express Co. v. Minnesota,* 223 U. S. 335, 344-5, it was said:

"The right of the State to tax property, although it is used in interstate commerce, is thoroughly well settled. *Postal Telegraph Co. v. Adams,* 155 U. S. 688; *Pullman's Palace Car Co. v. Pennsylvania,* 141 U. S. 18; *Ficklen v. Shelby County,* 145 U. S. 1, 22. • • •

" 'By whatever name the exaction may be called, if it amounts to no more than the ordinary tax upon prop-

erty or a just equivalent therefor, ascertained by reference thereto, it is not open to attack as inconsistent with the constitution.' *Postal Telegraph Cable Co. v. Adams*, 155 U. S. 688, 697."

These lieu taxes of Minnesota and other states, it must be remembered, were not sustained or sustainable on the theory that gross receipts is a proper criterion of property values. Such a holding would have been entirely out of harmony with *Johnson v. Wells Fargo & Co.*, 239 U. S. 234, holding invalid the valuation of the property of an interstate utility company by giving controlling effect to the gross income derived therefrom, and with the Minnesota Rate Cases, 230 U. S. 352, 458, condemning the apportionment of the value of the property of an interstate railroad used in its intrastate and interstate operations according to the gross income received from the two activities.

Such lieu taxes were sustainable, therefore, only on the theory that the tax imposed on gross income was no greater than that which would have been imposed, had the expense of state government been apportioned to these interstate utilities on an *ad valorem* tax basis.

By its New Tax Plan, the State of Washington has seen fit to distribute a part of the governmental costs to appellants and all other property owners on an *ad valorem* property tax basis, and to apportion the remainder of such costs of government according to the gross income received from practically all business activities, including the intrastate receipts of interstate utility companies.

And we respectfully submit that in determining whether appellants' interstate commerce has been unlawfully burdened by Washington's New Tax Plan, the

same test should be applied as in the cases sustaining a tax on interstate companies measured by gross income in lieu of a property tax, and that in the absence of a showing that the total tax burden thus imposed, property and excise, is not greater than that which would have been imposed had the State chosen to apportion the entire cost of government according to the relative value of the taxpayers' properties, it cannot be said that the excise thus exacted in lieu of taxes which might otherwise have been lawfully imposed as an added burden on property, is violative of the commerce clause.

It is of course apparent that a tax levied on an interstate carrier's tangible property and franchises is no less a burden on its interstate business than is a privilege tax measured by its intrastate gross income.

In this connection, may we note the language of Mr. Justice Stone, with Justices Holmes and Brandeis concurring, in *Helson v. Kentucky*, 279 U. S. 245, 252, wherein the majority held a tax on gasoline used in an interstate ferry to be void as violative of the commerce clause:

"I cannot yield assent to the reasoning by which the present forbidden tax on the use of property in interstate commerce is distinguished from a permissible tax on property, measured by its use or use value in interstate commerce. * * * (citing authorities) * * * Nor can I find any practical justification for this distinction or for an interpretation of the commerce clause which would relieve those engaged in interstate commerce from their fair share of the expense of government of the states in which they operate by exempting them from the payment of a tax of general application, which is neither aimed at nor discriminates against interstate commerce. 'It affects commerce among the States and impedes the transit of persons and property from one State to another just in the same way, and in

no other, that taxation of any kind necessarily increases the expenses attendant upon the use or possession of the thing taxed.' *Deleware Railroad Tax,* 18 Wall. 206, 232."

That this view is not out of harmony with that now taken by this court is evidenced by the later cases of *Eastern Air Transport v. Tax Commission,* 285 U. S. 147, *Nashville, C. & St. L. Ry. v. Wallace,* 288 U. S. 249, and *Edelman v. Boeing Air Transport,* 289 U. S. 249, holding that a state non-discriminatory use tax may constitutionally be imposed on gasoline imported and stored by an interstate carrier for use in generating motive power for instrumentalities of interstate transportation.

Distinguishing *Helson v. Kentucky,* 279 U. S. 245, Your Honors said in the *Wallace* case:

"But interstate rail carriers are not wholly immune from other forms of non-discriminatory state taxation, even though the burden of the tax is thus indirectly or incidentally imposed upon the interstate commerce in which they are engaged." (288 U. S. 267.)

That no distinction is to be made between property taxes and excises with respect to the taxation of the subjects, as distinguished from the instrumentalities, of interstate commerce, was held in *Wiloil Corporation v. Pennsylvania,* — U. S. —, 79 L. Ed. 382, where a non-discriminatory sales or use tax on liquid fuels was sustained as to gasoline sold within, but delivered from without, the taxing state.

"It is not material," said Your Honors there, "whether the tax is upon the sale and delivery or upon the property." (79 L. ed. 384.)

It must follow that if, as a result of the State's present scheme of taxation, "taken in its totality," the interstate carrier's total tax burden is not increased,

but *actually lightened* as compared with the tax burden which might legitimately be imposed by the taxing state, such interstate carrier cannot be heard to complain that its interstate business is unduly burdened.

In *Southern Ry. Co. v. Watts,* 260 U. S. 519, 530, the court said:

"It is argued that this franchise tax is an additional property tax which is not imposed on others, and that, consequently, it violates the uniformity clause of the state constitution and the equal protection clause of the Federal Constitution. It is true that the franchise tax is measured by the value of property already subjected to the *ad valorem* tax. But a privilege tax is not converted into a property tax because it is measured by the value of property (compare *Clark v. Titusville,* 184 U. S. 329, 333, 334); nor by the fact that in this measure is included property not used in the transportation service. Railroads differ in so many respects from other properties that they may, as a class, be taxed differently or additionally, if that is not inconsistent with the constitution of the state.

"Nor is there any basis for the claim that the franchise tax act violates the commerce clause. The tax appears to be upon the privilege of doing an intrastate business. Compare *Armour Packing Co. v. Lacy,* 200 U. S. 226. It is not of the character which is held a burden upon interstate commerce. *St. Louis Southwestern Ry. Co. v. Arkansas,* 235 U. S. 350; *Underwood Typewriter Co. v. Chamberlain,* 254 U .S. 113, 119, 120; *St. Louis-San Francisco Ry. Co. v. Middlekamp,* 256 U. S. 226. Payment of the tax is not made a condition precedent to granting a railroad permission to do interstate business. Compare *Leloup v. Mobile,* 127 U. S. 640. *Underwood Typewriter Co. v. Chamberlain,* 254 U. S. 113, 119. *And there is no basis for the contention that the aggregate burden imposed by the property tax, the franchise tax, and the income tax, operates to obstruct interstate commerce.*" (Italics ours.)

STATE'S NEW TAX PLAN:

Prior to 1932 practically the entire cost of government, state, county and municipal, was raised by *ad*

valorem taxes imposed on real and personal property including that of interstate carriers. By measures adopted by the people themselves at the general election of November, 1932, and by the people's representatives at the legislative session of 1933, this scheme of taxation was changed by shifting a substantial part of this burden of governmental expense from property to various kinds of businesses and occupations. Thus, by an initiative measure (Chap. 4, Laws of 1933) it was provided that thereafter (except when authorized by special elections) no more than 40 mills should be thereafter levied on the assessed valuation (50% of the actual value) of real and personal property, such millage being limited to 5 mills for the state, 10 mills for counties, 10 mills for school districts and 15 mills for cities or towns.

At the same election, the people, by direct vote, enacted a state income tax law (Chap. 5, Laws 1933) providing for a tax of certain percentages of all net incomes of individuals and corporations in excess of certain stated amounts. Although this income tax measure was later adjudged unconstitutional (see *Culliton v. Chase,* 174 Wash. 363), the court may nevertheless refer to its recitals to discover the people's purpose in adopting both the 40-mill and income tax measures. To quote:

"Existing methods of taxation, primarily based on property holdings, are inadequate, inequitable and economically unsound. Present conditions point the need of a new subject matter for taxation, which should be based on the ability to pay. Earnings for a given period are a fair measure of such ability.

"The people of the State of Washington, therefore, exercising herein their supreme power and fundamental right, declare their purpose hereby to tax all annual incomes within the state as such, and not as property." (Laws 1933, ch. 5, sec. 1.)

These two acts were initiative measures. At the following legislative session Chapter 28, Laws of 1933, was enacted, Section 4 of which limits the levy for the current school fund (a state fund theretofore unlimited) to five mills. The same session enacted Chapter 191, Laws of 1933 (the law here assailed), imposing an occupational tax on those engaged in various business activities, thereby largely shifting the expense of government from tangible property to such businesses and occupations.

REDUCTION IN RAILROADS' TAXES BY STATE'S NEW TAX PLAN:

At the trial of the railroad cases, appellee introduced exhibits for the purpose of comparing the total taxes, *ad valorem* and occupational, payable by the four large interstate railroads of the state for each of the years 1933 and 1934 (assuming such occupational tax to have been collectible for all of 1933, instead of only for the last five months), with the taxes which would have been payable by such railroads for such years under the revenue laws in effect prior to November, 1932. (Plff's Exs. "43" and "44," NP Rec. 224-226; Plff's Exs. "32" and "33," GN Rec. 241-244), which exhibits are explained by State's witness, Manschreck. (NP Rec. 194-6; GN Rec. 208-211.)

These exhibits are, we believe, self-explanatory, and show that as a result of the New Tax Plan the total taxes payable by the four roads (including the occupational tax) were $597,770 less in 1933 and $549,034 less in 1934 than they would have been under the old tax plan (see lines "A" to "H"), and that such companies' state taxes alone, plus the occupational tax, were $738,248 less in 1933, and $826,343 less in 1934 than such state taxes

alone would have been for those years under the old tax plan. (See lines "I" to "M.")

Had the 40-mill tax limit act been combined with the occupational tax measure it is clear that in determining whether such single tax measure imposed an undue and unlawful burden on appellents' interstate operations, the Court's first inquiry would necessarily have been as to the net results of the operation of such law in increasing or reducing such carriers' aggregate tax burden.

Suppose that, instead of the 40-mill act, the people or their legislature had adopted a measure freeing property from ALL *ad valorem* taxes, shifting the entire burden to businesses and occupations, and thereby substantially reducing the total taxes payable by the appellant railroads. Could these carriers then, while accepting such exemption features, be heard to urge that they should likewise escape the occupational tax and thus avoid any contribution whatever to the support of government? We submit not.

Our position is supported by *Chicago, M. St. P. & P. R. Co. v. Hedges*, 5 Fed. Supp. 752, 756, *et seq.*, where Judge Neterer said:

"To change its taxing system, the electors of the state, by initiation, adopted chapters 4 and 5, pp. 47, 49, Laws of Washington 1933 (40-mill levy limit on real estate and the income tax measure), and the Legislature, the act in issue, an 'emergency measure,' as a new taxing system. The preamble to chapter 5, p. 49, Laws of 1933, exposes the state of mind as follows:

" 'Existing methods of taxation, primarily based on property holdings, are inadequate, inequitable and economically unsound. Present conditions point the need of a new subject matter for taxation, which should be

based on the ability to pay. Earnings for a given period are a fair measure of such ability.

"'The people of the State of Washington, therefore, exercising herein their supreme power and fundamental right, declare their purpose hereby to tax all annual incomes within the state as such, and not as property.' Laws 1933, ch. 5, p. 49, Sec. 1.

"The Supreme Court of the state held this Income Tax Law unconstitutional [(*Culliton v. Chase, McKale's Inc. v. Chase*), 25 P. (2d) 81], and thus deprived the state of a portion of its revised system, and further disorganized the revenue situation. The 40-mill limit tax on real property authorized by chapter 4, p. 47, Laws of 1933, is grossly inadequate and the need of the 'emergency measure', and the act in issue, chapter 191, p. 869, Laws of 1933, effective from August 1, 1933, to July 31, 1935, became vital; and, in considering this issue, chapter 166, p. 613, Laws of 1933, should be noted. • • •

"Consideration of the new system to supersede the old, and the status of the litigants under the old system, and the traffic rates approved by the rate-making body, the Interstate Commerce Commission, which must be presumed as sufficient for interstate commerce, is enlightening. May it be said that any burden has been placed on interstate commerce by the challenged act, when, as later particularized, the new system, including the excise law (term used merely for designation) in issue, commerce, intra and inter state, has been relieved of $737,825 taxes?

"The principle that these laws must be considered together is approved in *Baker v. Druesedow*, 263 U. S. 137, 44 S. Ct. 40, 68 L. Ed. 212, and cited cases; *Greene v. Louisville & I. R. Co.*, 244 U. S. 499, 37 S. Ct. 673, 61 L. Ed. 1280; *Gregg Dyeing Co. v. Query*, 286 U. S. 472, 52 S. Ct. 631, 76 L. Ed. 1232, 84 A. L. R. 831. If the state has not by all of its taxation legislation, burdened interstate commerce, it may not be criticized. *Hebert v. Louisiana*, 272 U. S. 312, 47 S. Ct. 103, 71 L. Ed. 270, 48 A. L. R. 1102; *Lindsley v. Natural Carbonic Gas Co.*, 220 U. S. 61, 31 S. Ct. 337, 55 L. Ed. 369, Ann. Cas. 1912C, 160. • • •

"The plaintiffs are receiving all of the revenue they received prior to the act in issue, with no added burden on interstate commerce, or at all. No burden could be

placed upon interstate commerce by the changed taxing system, if the tax has been lessened and no reduction of tariff rates made, as in this case.

* * * * * * * * *

"* * * Obviously complainants 'suffer no harm from the provisions of the statute.' *Osborne v. Florida*, 164 U. S. 650, 17 S. Ct. 214, 216, 41 L. Ed. 586. The net saving to the complainants, under the new system, including the excise tax, is $737,825. The excise tax is in no event a direct charge against interstate commerce, and, if it indirectly affects it, it is not forbidden. *Oliver Iron Co. v. Lord*, 262 U. S. 172, 43 S. Ct. 526, 67 L. Ed. 929; *State v. Express Co.*, 80 Wash. 309, 141 Pac. 757.

"This does not take cognizance of benefits to the complainants of the Motor Truck Act (chapter 166, p. 613, Laws 1933), curtailing truck competition and increasing the traffic revenues for the complainants' roads. Instead of taking from other states and contributing to the state of Washington, as contended by complainant in argument, there is actually taken from the taxpayer and patrons of the complainants' roads in the state of Washington $737,825 to apply in other states. Assuredly, complainants may not invoke the Fourteenth Amendment. *Gant v. Oklahoma City*, 289 U. S. 98, 53 S. Ct. 530, 77 L. Ed. 1058. * * *."

"But," appellants argue, "we are required to pay the same *ad valorem* taxes as are imposed on all other property, and on top of that, an excise not exacted of other tax payers."

But this argument, we submit, is patently fallacious. Let us consider, for instance, the total revenue received by the State under its New Tax Plan from the valuable business properties in its larger cities. It receives, first, the *ad valorem* tax exacted of the owner, and in addition, the business or occupational tax exacted of every business enterprise conducted on such business property. From such properties as public stages, trucks, ferries, etc. it first exacts an *ad valorem* tax on the vehicles themselves and on the owners' franchises, and in addi-

tion, an occupational tax measured by the intrastate gross receipts from such activities.

And in this connection we would call particular attention to the fact that although the property of municipal corporations is expressly exempted from *ad valorem* taxation by Article VII of the State constitution, the offending occupational tax is imposed on municipalities operating public utilities and conducting businesses, the same as upon private enterprises (Laws 1933, ch. 191, Sec. 2-e), which provisions have been sustained by the State court. See *Tacoma v. State Tax Commission,* 177 Wash. 604. Needless to say, no small part of the burden of taxation is thus shifted from appellants' property to municipally owned street railways, and water, light and power plants not otherwise taxable.

That the total burden of taxation thus imposed has, as a necessary result of the State's New Tax Plan, been shifted from the appellant companies to these municipalities and to the business carried on in connection with the other general taxable property of the State, is, we submit, conclusively demonstrated by the fact that such appellants' entire tax burden, *ad valorem* and excise, is now materially less than it would have been under the former method of requiring taxable property to bear the entire load.

Counsel profess concern that if the 1933 tax be sustained, the state legislature may raise the rate to 10, 25 or even 50%.

The answer is three-fold: (a) it cannot be presumed that the State will attempt to tax these roads out of existence; (b) appellants' patrons who must ultimately pay the tax would not tolerate an unreasonable

exaction; and (c) should counsel's fears be realized, the courts will on application, promptly declare such an unreasonable and discriminatory imposition invalid as violative of the constitutional provisions which appellants now seek to invoke.

Since the 1933 measure was adopted, the sorely pressed State legislature has twice convened, but has not raised the rate as to railroads beyond that originally imposed on several other utilities including telephone companies, but instead, has exacted of the State's citizens a 2% retail sales tax to meet the emergency. (Laws 1935, Ch. 180.)

EFFECT OF NEW TAX PLAN ON APPELLANT, TELEPHONE COMPANY:

This company has received all the benefits of a tax reduction on its property, without necessarily suffering from the imposition of the occupational tax. It concedes that it is making at least some net returns on the fair value of its property used in its intrastate operations. (PT Rec. 4.) There are no competitive companies in the field which it occupies. (PT Rec. 68.) It neither alleged nor proved that its rates could not be so increased as to cover the excise exacted without loss of patronage. Yet it also concedes that it has made no application to any regulatory body, state or federal, for an increase of its rates for the purpose of meeting the tax. (PT Rec. 100.)

There is nothing in the Occupational Tax Act which prevents it from passing the tax on to its patrons.

Not only does the State court in effect so hold in the cases before us, but in *State ex rel. Stiner v. Yelle*, 174 Wash. 402, 410, it was said:

"Moreover, the farmer cannot pass the tax to the

ultimate consumer, while all those later dealing with his products, like all others engaged in commercial pursuits, may and probably will very largely do so."

And in *Cascade Telephone Co. v. State Tax Commission,* 176 Wash. 616, the court, if it did not squarely so hold, at least strongly implied that the fact that the Governor vetoed the section of the Act *requiring* the taxpayer to pass the tax along to the ultimate consumer, did not prevent the taxpayer from doing so if he chose. A similar suggestion is found in *Tacoma v. State Tax Com.,* 177 Wash. 604, 611.

Indeed, none of the appellants even suggest that there is anything in the Act even impliedly forbidding that the tax be passed along to appellants' customers.

"To add by implication" said Your Honors in *American Express Co. v. Michigan,* 177 U. S. 404, 412, "such a provision to a tax law would be contrary to its intent, and be in conflict with the general object which a law levying taxes is naturally presumed to effectuate."

If on application to the proper authority, the P. T. is allowed (and we have no reason to doubt but that such permission would be granted) to increase its rates to the extent of the tax exacted, obviously that company would be in the position, not of a taxpayer, but of a mere tax collector, and neither its intrastate nor interstate operations would be burdened thereby.

For the reasons so clearly set forth in *Postal Tel.-Cable Co. v. Fremont,* 255 U. S. 124, 217-8, and *Postal Tel.-Cable Co. v. Richmond,* 249 U. S. 252, 258, we submit that so far as the P. T. is concerned, the tax is an invasion of neither the due process nor the commerce clause of the federal constitution.

In *Postal Tel.-Cable Co. v. Fremont,* 255 U. S. 124,

it was contended, as here, that the complaining company was required by State law not only to continue to engage in intrastate business, but at designated rates, but the court said:

"The company, as we have seen, cites Sec. 7408 as a compulsion upon it to engage in intrastate business and at designated rates. From the rigor of the requirement Sec. 7409 provides a mode of relief, and until it is denied the company cannot complain under the circumstances presented by this record. In other words, if Sec. 7408 is imperative upon the company to continue intrastate business, Sec. 7409 affords a means of obtaining relief from burdensome obedience. The sections are counterparts. If submission to Sec. 7408 results in insufficient revenue and a burden upon interstate commerce, it is made the duty of the Railway Commission by Sec. 7409 upon complaint of the Postal Company to raise the intrastate rate 'fixed' in Sec. 7408. No attempt to secure relief under Sec. 7409 appears to have been made."

DISCUSSION OF APPELLANTS' SPECIFIC OBJECTIONS TO 1933 OCCUPATIONAL TAX ACT:

The N. P.'s and G. N.'s assignments of error are substantially identical and are to the following effect:

(1) That having held as a matter of law that appellant cannot withdraw from its intrastate business without also withdrawing from its interstate business, the State court erred in holding said tax not to be violative of the commerce clause;

(2) That having held that as a practical matter appellant cannot withdraw from its intrastate business without also withdrawing from its interstate business, said court erred in holding said tax not to be violative of the commerce clause;

(3) That having found that the appellant's intrastate business is conducted at a loss which must be borne by its income from interstate business, said court erred

in holding said tax not to be violative of the commerce clause and due process clause.

(4) That having found that the appellant's intrastate business is conducted at a loss which must be borne by its income from interstate business, said court erred in holding that the tax was not violative of the commerce clause for the stated reason that the appellant had not exhauted its remedy (by writ of review) to obtain intrastate rate increases, for the reason that such circumstance is immaterial, and not supported by, but contrary to the facts found by the trial court.

The P. T.'s assignments of error are the same as the first two above set forth, to which it has added the following:

(5) That having found that the P. T. cannot, as a matter of law, retire from its intrastate business while continuing its interstate business, the court erred in holding the tax not to be violative of the due process clause.

THE TRIAL COURT'S FINDINGS IN THE N. P. AND G. N. CASES WERE NOT ADOPTED BY STATE SUPREME COURT:

At the outset it is important to note that appellants' various assignments of error are based upon wholly erroneous assumptions. The state supreme court did not hold as to any of the appellants, that it could not, as a matter of law, retire from its intrastate business without also retiring from its interstate business. Neither did it find from the evidence as to any of the appellants that, as a practical matter, such appellant could not retire from its intrastate business without also retiring from its interstate business, or that either railroad com-

pany was conducting its intrastate business at a loss. On the contrary, without passing upon the merits of any of these contentions, the court, for the purpose of argument, merely *assumed* them to be well-taken, and then proceeded to hold each and all of them immaterial and to sustain the tax. This is obvious from the following language of the court:

"The next and, as we view it, the important and difficult question is whether the tax may be collected, even though the railway company, the respondent, may not be able to retire from its intrastate business without also discontinuing its interstate. In this connection, *it will be assumed* (a) that the respondent cannot, as a matter of law, retire from its intrastate business; (b) that it is impractical, as a matter of fact, for it to retire from its intrastate business without also retiring from its interstate; and (c) that the intrastate or local business is conducted at a loss which is taken care of by the receipts from the interstate business. Giving effect to these *assumptions,* inquiry must be directed then to whether the tax is valid, even though the railway company may not be able to retire from its intrastate business without retiring from its interstate, and that the intrastate business is conducted at a loss." (Italics ours.) *State v. N. P. Ry. Co.,* 83 Wash. Dec. 52, 55, 48 Pac. (2d) 931, NP Rec. 57.

But counsel for appellant railroads would have Your Honors believe that the State supreme court adopted the findings of the trial court as its own, such contention being based, apparently, upon the court's following statement in its opinion in the N. P. case:

"As found by the trial court, the interstate and intrastate business in this state is inextricably commingled, and the intrastate business is conducted at a loss, and it is necessary to make up this loss from the income

from interstate business." *State v. N. P. Ry. Co.*, 83 Wash. Dec. 52, 53, 48 Pac. (2d) 931, NP Rec. 55.

But it is perfectly apparent that in using this language the court was merely reciting what the trial court had found. Surely, where the State supreme court reached the conclusion that the offending tax was valid without regard to the trial court's findings, this court cannot assume that, by the above recitals, the State supreme court intended to adopt the trial court findings on these hotly contested issues. It must be remembered that the State had assigned numerous errors based on the trial court's findings on these issues and on the admissibility of the evidence upon which they were seemingly based. (Post, pp. 93-180.) The State court could not, we submit, have intended to overrule all of these numerous assignments without making any reference to them whatever.

Section 2, Article IV, of the State Constitution provides:

"In the determination of causes, all decisions of the court shall be given in writing, and the grounds of the decision shall be stated."

Surely, it should require the most positive and unequivocal language, to persuade Your Honors that the State supreme court had so grievously violated its plain constitutional duty.

Again, we find no such recital in the court's opinion in the G. N. case. See *State v. G. N. Ry. Co.*, 83 Wash. Dec. 66, 48 Pac. (2d) 938, GN Rec. 84.

Moreover, in the P. T. case, an equity cause, in which the lower court made no findings, and in which the complaint expressly alleged that the P. T. was making

a net profit on its intrastate business (PT Rec. 4), we find the State supreme court basing its decision upon its opinion in the N. P. case (*Pac. Tel. & Tel. Co. v. State Tax Commission,* 83 Wash. Dec. 67, 48 Pac. (2d) 938, PT Rec. 151), with no reference whatever to the trial court's findings.

In view of fact, then, that in reaching its conclusions on the law, the State supreme court merely *assumed* that it was impractical for the N. P. to withdraw from its intrastate business, and that it was conducting such intrastate business at a loss, the court's opinion, must, we submit, be construed as a mere recital, but without endorsement, of the trial court's findings. Nothing more.

Disposition of appeals if assumptions found material.

What disposition, then, should be made of these appeals should Your Honors conclude that the tax would be invalid on the basis of an assumption that the appellants cannot, as a matter of law, retire from their intrastate business without also retiring from their interstate business?

The correctness of this assumption necessarily involves purely a construction of the local constitution and statutes, as to which the State supreme court's decision is controlling. Consequently, if the correctness of this assumption is found to be material, it would seem that Your Honors should not attempt to decide this question of local law, but should make such disposition of the appeals as to permit the State supreme court to exercise its undoubted prerogative in this regard. *Clark v. Williard,* 292 U. S. 113, 128-9.

But if, as we contend, the Washington constitution and statutes would themselves be violative of the com-

merce clause if given the assumed construction, then obviously this assumption of the State court should be wholly disregarded, since it would be wholly useless and ineffectual for the State court to reach a conclusion which would in and of itself, wholly vitiate such state statutes and constitutional provisions.

APPELLEE'S OBJECTIONS TO TRIAL COURT'S FINDINGS AND RULINGS ON ADMISSIBILITY OF EVIDENCE IN N. P. AND G. N. CASES.

In its appeals to the State supreme court in each of these cases, the appellee here, as appellant there, assigned numerous errors both as to the propriety of the trial court's findings, and as to the admission of evidence received in support of the same. May we note that in its designation of additional portions of the record to be printed in the N. P. and G. N. cases (NP Rec. 325-6; GN Rec. 293-4), the appellee requested that the clerk print those portions of its State court briefs setting forth its assignments of error. While these assignments are printed in the G. N. transcript (GN Rec. 79-83), we fail to find them in the N. P. transcript, but since they appear in the unprinted record and are set forth herein, we assume that this court will notice them.

Under the Washington practice, the complaining party may base error upon adverse findings without the necessity of taking exceptions thereto in the trial court. (NP Rec. 77; GN Rec. 108) But in the appellant's brief, each error relied upon must be clearly pointed out and separately discussed. (NP Rec. 76; GN Rec. 108)

Appellee's purpose in requesting that such assignments be certified to this Court was to show that it had assigned error in the State supreme court based on these various adverse findings and rulings of the trial court,

which assignments the court had failed to consider for the reason that, to sustain the offending tax, it was found unnecessary to do so. This appellee believed necessary not only to advise Your Honors that appellee had not acquiesced in the trial court's findings and rulings, but to show that if such findings were deemed material, appellee was entitled to have the same reveiwed either by this Court, or to have the causes remanded for that purpose to the State supreme court.

Of course, should Your Honors follow any other course, it would mean that the State would be wholly deprived of its unquestioned right to have these adverse findings and rulings of the trial court reviewed either by this or the State supreme court.

Upon an appeal from a decree of the Supreme Court of the Philippine Islands erroneously reversing the trial court solely on a question of law, this Court held in *Philippine Sugar &c. Co. v. Philippine Islands,* 247 U. S. 385, that, in order to dispose finally of the case, Your Honors might review the facts, when all the evidence proffered was admitted, and was in the record, and where the appellant in the court below sought to review the trial court's findings.

The Court will find the evidence on the question of whether or not the appellant railroads are in fact losing money on their local business, and the trial court's adverse rulings on the admissibility of evidence relating thereto, reviewed at length in Appendix "A" (Post, pp. 93-151) as to the N. P., and in Appendix "B," (Post, pp. 152-180) as to the G. N.

EVIDENCE AS TO N. P. AND G. N. NET EARNINGS IN INTRASTATE BUSINESS IN 1933.

The Northern Pacific:

The undisputed evidence showed that instead of losing $413,866 as claimed, had the N. P. computed its passenger operating expense on the same basis as the G. N., its net earnings would have been $87,710; and having made this correction, had it apportioned taxes on a relative use basis as required by the *Minnesota Rate Cases*, 230 U. S. 352, instead of on a relative gross revenue basis, its net earnings would have been $285,131; and having made these corrections, had it correctly apportioned traffic expenses, and not charged pensions as an operating expense, its net earnings would have been $457,160. Having made these corrections, had the N. P., in its calculations, used the intrastate revenues reported to the D. P. W., its net earnings would have been $583,154. (Post, pp. 140-1.)

The Great Norhern:

The undisputed evidence showed that by its own calculations, by using the intrastate revenues reported to the D. P. W., its net earnings were $202,458, and not deducting car and joint facility rentals as an operating expense, its net earnings were $491,544. (GN Ex. "11," p. 1, GN Rec. 258.)

But making the full deductions from its reported revenue as claimed, and not deducting car and joint facility rents as an operating expense, its net earnings were $114,152. (GN Ex. "11," p. "A," item 5, GN Rec. 254.) And even making such deductions from revenue and deducting such car and joint facility rents as an operating expense, but correctly apportioning taxes and joint facility rents, eliminating pensions as an oper-

ating expense, and eliminating duplications of expense, its net earnings were $132,256. (Post, pp. 175-6.)

G. N. AND N. P. CONCEDED A SUBSTANTIAL PROFIT FROM THEIR INTRASTATE FREIGHT BUSINESS.

The N. P. admittedly made a profit of $729,940 on its intrastate freight business, but claimed to have absorbed such profits in its claimed net loss of $1,143,806 on its passenger business with a resulting claimed net loss on the two activities combined of $413,866. (Post, pp. 141-3.)

The G. N., on its most extreme calculations, admittedly made a profit of $430,234 on its intrastate freight business, but claimed to have absorbed such profits in its claimed net loss of $529,503 on its passenger business with a resulting claimed net loss on the two activities combined of $99,269. (Post, pp. 176-8.)

Surely it cannot be seriously contended that any valid statute or constitutional provision, either state or federal, can compel an intrastate carrier to continue its intrastate passenger business, every dollar of revenue from which costs the carrier $1.95 (as the G. N.), and $3.66 (as to the N. P.). See *Railroad Commission v. Eastern Texas R. R.*, 264 U. S. 79.

And if such carrier elects to continue such losing local passenger business, why, we ask, charge the loss to its local freight profits, rather than to its system passenger business to which its local passenger business is at best, merely incidental?

For the purpose of this inquiry, should not these carriers' passenger and freight operations, we ask, under the circumstances here revealed, be treated as separate and distinct business activities for the purpose of determining the validity of the offending tax?

RAILROAD APPELLANTS' CONTENTION THAT OCCUPATIONAL TAX ACT INVALID AS TO THEM, IF THEIR INTRASTATE BUSINESS IS CONDUCTED AT A LOSS.

We submit that under the facts revealed by the record the State supreme court was absolutely correct in not condemning the tax on the ground urged. To quote the language of the court:

"But it is said that the intrastate business is being conducted at a loss, and this loss must be borne by the interstate business and therefore is a burden upon interstate commerce. There is an expression in the case of *Postal Telegraph-Cable Co. v. Richmond*, 249 U. S. 252, 39 S. Ct. 265, that would appear to support this contention, even though the question was not necessarily involved in that case; and further, in that case there was not involved an excise tax based upon gross income, as here.

"In this state, if the respondent's intrastate business is conducted at a loss, the legislature has provided a remedy, first, by application to the department of public service, with the right of review by the superior court and an appeal to this court. From the findings, it appears that an application has been made and denied by the department, and that another application is pending. It does not appear, however, that the respondent has exhausted the relief granted by the statute, and until it does so, it cannot be said that, even though the intrastate business is being conducted at a loss, it is such a burden upon interstate commerce as would justify holding the law unconstitutional.

"The facts in the case of *Postal Telegraph-Cable Co. v. Fremont*, 255 U. S. 124, 41 S. Ct. 279, presented a similar question, and it was there held that, where the state law affords a means to prevent the tax from burdening interstate commerce, through an application to increase intrastate rates, the tax will not be held void, in the absence of a showing that the company had exhausted the remedy afforded by an increase of the rates on intrastate business. We see no just or legal reason why the respondent should not comply with chapter 191, as all other businesses in this state are required to do." *State v. N. P. Ry. Co.*, 83 Wash. Dec. 52, 61-2, 48 Pac. (2d) 931; NP Rec. 54, 62.

The court recites, it will be noted, that "from the findings, it appears that an application" (for an increase in local tariffs) "has been made and denied by the department, and that another application is pending."

But it definitely appears from counsel's own admissions that neither the N. P. nor G. N. has ever sought an increase of rates from either the D. P. W. or the I. C. C. *by reason of the imposition of the occupational tax.* Thus, speaking of the showing made by the N. P. and G. N. in certain rate investigations pending before each of those bodies, counsel for the N. P. said:

"There was no occupational tax included, because none had ever been levied against the railroad, much less collected, and we don't think any will ever be collected, either. So it certainly was not in the showing." (NP Rec. 154; GN Rec. 200.)

And in the rate proceeding instituted by these roads before the D. P. W. in September, 1934, the railroads did not make any claim based on the occupational tax. (NP Rec. 155; GN Rec. 200.)

Thus the records reveal that far from petitioning these regulatory bodies for an increase of rates to meet the occupational tax, they have always taken the position that such tax is void as to them.

True, each of these carriers alleged in its answer (NP Rec. 13; GN Rec. 19), and secured a finding of the trial court (NP Rec. 50; GN Rec. 73) to the effect that most of its local rates cannot be raised, because of competitition from other kinds of transportation. But there is, we submit, not a syllable of evidence in the record to justify any such finding.

The "competition" referred to, is no doubt highway

transportation companies, but the same tax imposed on railroads is likewise exacted of truck lines. (Laws of Wash. 1933, Ch. 191, Sec. 2(2)(e)XI.) May it not therefore be fairly assumed in the absence of evidence to the contrary, that these competitors have met with the same problem as these appellants as to the necessity of a rate increase to meet the tax. Indeed, the problem of the trucks is all the more pronounced in that their total tax burden is very materially increased by the New Tax Plan whereas that of the railroads, as we have shown, is materially lightened.

The only evidence offered by these roads in support of their allegations of inability to raise *many* of their local rates, was an order of the D. P. W. dated April 27, 1933, denying the carriers' application made January 13, 1933, for an order extending to September 30, 1933, a 15% local rate increase then in effect, to September 30, 1933 (NP Rec. 14-16; GN Rec. 21-23), which order recited that it was a matter of common knowledge that "the present level of rail rates is too high to permit freedom of movement by rail."

But it is apparent that the rates to which the commission referred were the rates which had been in effect up to March 30, 1933, but a few days before such order was entered. It would have had no occasion to speak of any other rates.

Moreover, the effect of the order was to deny a 15% increase. To meet the occupational tax, only a 1½% increase would have been necessary. There is nothing in the order to indicate that the D. P. W. had any occasion to consider the effect of the occupational tax. Nor could it have had, since the order was made in April, 1933, and

the Tax Act did not take effect until August 1, 1933,

It must follow that any statements made in this order relative to the existing rates being as high as the traffic would bear, could not have been made in the light of the imposition of the occupational tax, which would fall as heavily, if not more heavily on the railroads' competitors than on the railroads themselves.

It would not follow, we submit, that because the local traffic would not bear a 15% rate increase, these carriers would have lost patronage because of a 1½% increase in rates.

But the most persuasive reason why any recitals in this order are wholly immaterial is that it is obviously directly opposed to the railroads' own position in these proceedings. If these carriers honestly believe what they allege in their answers, that not many of their local rates can be increased on account of competition, then *why were they before the D. P. W. in April, 1933, petitioning for an increase in such rates? And why, in September, 1934, were they again before the D. P. W. and I. C. C. seeking such an increase?* [NP Rec. 155; GN Rec. 200.]

These carriers cannot, we submit, be heard to assert in one proceeding that the facts justify an increase in their local rates and in other proceedings taken but a few weeks before the trial of these cases, that such increases are wholly unwarranted.

Nor, as already pointed out (Ante, pp. 35-36) is there anything in the Occupational Tax Act indicating a legislative purpose to forbid the public service companies so taxed from thus shifting the burden by an increase of rates. See *State ex rel. Stiner v. Yelle,* 174 Wash. 402,

410; *American Exp. Co. v. Michigan,* 177 U. S. 404, 412-3, and other cases heretofore cited.

The appellant railroads, having never applied to any regulatory body, let alone a reviewing tribunal, for permission to increase their rates *to meet the occupational tax,* cannot now be heard to assert that the same is a burden on interstate commerce either because they are doing local business at a loss, or that they are under legal compulsion to continue their intrastate operations. *Postal Tel.-Cable Co. v. Fremont,* 255 U. S. 124; *Postal Tel.-Cable Co. v. Richmond,* 249 U. S. 252; *Chicago, etc. R. R. Co. v. Hedges,* 5 Fed. Supp. 752, 759-60.

As shown in our review of the evidence bearing thereon, the record does not support these appellants' claim that in 1933 either of them actually conducted its intrastate business at a loss. (See post, pp. 35-6.) But if such a showing had in fact been made, there is nothing in the record to show that 1933 was representative of what was to be expected in future years. The G. N. made no attempt to show that its 1933 operations were representative, and from such showing as the N. P. attempted, it appeared that 1934 showed at least some improvement over 1933. (Post, pp. 148-151.) In *Williams v. Talladega,* 226 U. S. 404, 417, a eleven-months test period was held insufficient, and in *Postal Tel.-Cable Co. v. Fremont,* 255 U. S. 124, 126, a finding of the State Court that a two-year test period was insufficient was not disturbed. In his concurring opinion in *Chicago, etc. R. Co. v. Hedges,* 5 Fed. Supp. 752, 760, Judge Cushman said:

"The bills of complaint make no disclosure as to income and expense other than for the years 1932 and 1933. It was stated, in effect, upon the hearing, and not disputed, that no application had been made under the

Public Service Commission Law to increase rates.

* * * * * * * *

"Complainants' case is based upon the presumption that future results will be similar to those already experienced, but such presumption cannot be indulged where there have been so numerous, radical, and far-reaching changes. When such presumption obtains, it depends upon the existence and continuance of the applicable precedent conditions. Any determination now reached, it is clear, would be based upon little more than conjecture and speculation."

Inasmuch as the reasonableness of a rate depends upon whether or not it yields a fair return, the sum required to meet the operating expenses of the utility must be considered. Taxes to which the utility is subject in the performance of its public duties, including state taxes on earnings and federal income taxes are to be considered as part of its operating expenses.

51 C. J. 25;

Galveston Elec. Co. v. Galveston, 258 U. S. 388, 399;

Georgia Ry. v. R. R. Com., 262 U. S. 625, 633.

We submit that the Act is not vulnerable to attack by reason of the claimed present inadequacy of appellants' earnings from intrastate business.

CONTENTION THAT OCCUPATIONAL TAX ACT IS VIOLATIVE OF COMMERCE CLAUSE IF APPELLANTS, AS MATTER OF LAW, CANNOT RENOUNCE THEIR INTRASTATE BUSINESS WITHOUT ALSO WITHDRAWING FROM THEIR INTERSTATE BUSINESS.

Answering this contention, the State supreme court said (*State v. N. P. Ry. Co.,* 83 Wash. Dec. 52, 56, 48 Pac. (2d) 931, NP Rec. 54, 57-61):

"In the case of *Sprout v. South Bend,* 277 U. S. 163, 48 S. Ct. 502, 62 A. L. R. 45, the court had before it an ordinance of the city, in the state of Indiana, which prescribed license fees varying in amount depending upon

the seating capacity of a bus, the bus company being engaged in both intrastate and interstate business, and it was there held that 'the ordinance is void because of the imposition of the license fee.' In the course of the opinion, it was said that a state may, by appropriate legislation, require the payment of an occupation tax from one engaged in both intrastate and interstate commerce, but, in order that the fee or tax may be valid,

"'* * * it must appear that it is imposed solely on account of the intrastate business; that the amount exacted is not increased because of the interstate business done; that one engaged exclusively in interstate commerce would not be subject to the imposition; and that the person taxed could discontinue the intrastate business without withdrawing also from the interstate business.'

"It will be observed that one of the conditions there placed upon the right of a state to impose the tax is that the person or corporation taxed 'could discontinue the intrastate business without withdrawing also from the interstate business.' The last quoted expression, so far as we are informed, was first used in the case of *Pullman Co. v. Adams,* 189 U. S. 420, 23 S. Ct. 494, where the tax involved was in a specific amount, levied upon

"'* * * each sleeping and palace-car company carrying passengers from one point to another within the State, one hundred dollars, and twenty-five cents per mile for each mile of railroad-track over which the company runs its cars.'

"In the case of *Cooney v. Mountain States Tel. & Tel. Co.,*— U. S. —, 55 S. Ct. 477, there was involved a statute of the state of Montana prescribing a tax 'for each telephone instrument used in the conduct of the business of operating or maintaining telephone lines and furnishing telephone service in the state of Montana.' There, the telephone company, as is the railroad company here, engaged in both intrastate and interstate business, and it was held that a privilege or occupation tax which a state imposes with reference to both kinds of business, though an indiscriminate 'application to instrumentalities common to both sorts of commerce, has frequently been held to be invalid.'

"It will be observed that in none of the three cases mentioned was the tax based upon the gross income of the intrastate business. There is a difference between

a tax imposed as a license to do business or upon the instrumentality and a tax based upon the gross income. If the tax be a license tax or one upon the instrumentality, it necessarily inheres in the interstate as well as the intrastate business. Where the tax is upon the gross income, the income from the interstate business may be segregated from the intrastate and be held valid.

"In the case of *Bowman v. Continental Oil Co.*, 256 U. S. 642, 41 S. Ct. 606, the state of New Mexico had imposed an excise tax of two cents for each gallon of gasoline sold or used, and an annual license tax of fifty dollars for each distributing station or place of business. The oil company was engaged in both interstate and intrastate business. It was held that the two cents tax per gallon could be sustained because the income from the intrastate business could be segregated from the interstate, but that the fifty dollar tax was void because no such segregation could be made. It was there said:

" 'The applicable rule is that laid down in *Ratterman v. Western Union Telegraph Co.*, 127 U. S. 411, where, in response to a question whether a single tax, assessed by a state upon the receipts of a telegraph company derived partly from interstate commerce and partly from commerce within the State, but returned and assessed in gross and without separation or apportionment, was wholly invalid or invalid only in proportion and to the extent that the receipts were derived from interstate commerce, this court unanimously answered that so far as levied upon receipts derived from interstate commerce the tax was void, but so far as levied upon receipts from commerce wholly within the State it was valid. This case has been cited repeatedly with approval and its principle accepted. *Western Union Telegraph Co. v. Alabama*, 132 U. S. 472, 476-477; *Lehigh Valley R. R. Co. v. Pennsylvania*, 145 U. S. 192, 200-201; *Postal Telegraph Cable Co. v. Charleston*, 153 U. S. 692, 697; *Western Union Telegraph Co. v. Kansas*, 216 U. S. 1, 31.

" 'But with the license tax it is otherwise. If the statute is inseparable, then both by its terms and by its legal operation and effect this tax is imposed generally upon the entire business conducted, including interstate commerce as well as domestic; and the tax is void under the authority of *Leloup v. Port of Mobile*, 127 U. S. 640,

647; *Crutcher v. Kentucky*, 141 U. S. 47, 58-59; *Williams v. Talladega*, 226 U. S. 404, 419; and other cases of that character'.

"In the case of *Cooney v. Mountain States Tel. & Tel. Co., supra*, it was distinctly pointed out that the tax there involved was

"'* * * not laid on revenue derived from monthly rates as distinguished from toll charges. It is not imposed with respect either to the nature of the revenue, or to the character of the service from which the revenue is derived, or to the manner in which the charges for the service are fixed.'

"From what is there said, it would appear to be a reasonable inference that, if the tax were of the character described in the quotation just made from the opinion, the result might be different.

"In *East Ohio Gas Co. v. Tax Commission*, 283 U. S. 465, 51 S. Ct. 499, the state of Ohio imposed upon every corporation engaged in the business of supplying consumers within the state with natural gas for light, heat or power a tax based upon the gross receipts, and the law was sustained. The East Ohio Gas Company, which resisted the tax, was engaged both in interstate and intrastate business. It brought gas from the states of West Virginia and Pennsylvania over high pressure pipes, and, as stated in the opinion, this was interstate commerce until it reached the distributing pipes which supplied the consumers, and after that it became intrastate and was subject to the tax. In the course of the opinion in that case, we find the same statement with reference to the conditions precedent to the right of a state to impose a tax upon a person or corporation engaged in both intrastate and interstate business, as appears in the quotation from the case of *Sprout v. South Bend, supra*. In the *Ohio Gas Co.* case, however, the court did not apply the provisions that the gas company could not retire from its intrastate business without withdrawing from its interstate business. The facts, as they appear in the opinion, make it plain that, if the gas company had withdrawn from its intrastate business, it would have completely destroyed its interstate business. The tax there involved was not one upon the instrumentality or a license tax, but was an excise or a tax upon the privilege of doing business.

"The result of the holding in that case, as we view it, would sustain a holding in the case now before us that the tax upon the gross income of the intrastate business was valid, even though the railway company could not withdraw from that business without also withdrawing from its interstate business. We do not look upon cases which involve either a tax upon instrumentalities or a license tax as applicable to the law now in question, which imposes, as already indicated, an excise or tax on the privilege of engaging or continuing in business."

EVEN WERE APPELLANTS UNDER LEGAL COMPULSION TO CONTINUE THEIR INTRASTATE BUSINESS EVEN AT A LOSS, TAX WOULD NOT BE DEEMED AN UNLAWFUL BURDEN ON INTERSTATE BUSINESS UNTIL APPELLANTS HAD BEEN DENIED RATE INCREASES TO MEET TAX.

The same contention as made here by appellants, was made without success in *Postal Tel.-Cable Co. v. Fremont,* 255 U. S. 124, 128. May we here repeat the following language already quoted from that case:

"The company, as we have seen, cites § 7408 as a compulsion upon it to engage in intrastate business and at designated rates. From the rigor of the requirement § 7409 provides a mode of relief, and until it is denied the company cannot complain under the circumstances presented by this record. In other words, if § 7408 is imperative upon the company to continue intrastate business, § 7409 affords a means of obtaining relief from burdensome obedience. The sections are counterparts. If submission to § 7408 results in insufficient revenue and a burden upon interstate commerce, it is made the duty of the Railway Commission by § 7409 upon complaint of the Postal Company to raise the intrastate rate 'fixed' in § 7408. No attempt to secure relief under § 7409 appears to have been made."

True, here the revenue measure does not itself provide the machinery for an application for rate increases, but other regulatory measures do, and until appellants have exhausted the remedy thus afforded, they have no reason to complain.

It would, we feel, be an impertinence to attempt to add anything further to what has been so clearly stated by the State supreme court in this connection.

But we do not agree that there is any such legal obligation as the court assumes.

STATE SUPREME COURT HAS NOT CONSTRUED STATE STATUTES AND CONSTITUTION AS REQUIRING APPELLANTS TO RENOUNCE THEIR INTERSTATE BUSINESS IF THEY WITHDRAW FROM THEIR INTRASTATE BUSINESS.

As heretofore noted, in the present cases the State supreme court merely assumed such to be the law, for argument's sake. And obviously, if in other cases the State supreme court has not construed the State constitutional and statutes as thus assumed, appellants' contention must be without merit.

Appellants contend that under the Public Service Commission Law (Ch. 117, Laws of 1911) and Article XII, Sections 13, 14, 15, and 19, of the state constitution, they cannot withdraw from their intrastate activities while continuing to carry on their interstate business.

Before examining the local decisions, may we suggest that only the sovereign could complain should appellants elect to withdraw from their local business. No one, we submit, can question appellants' right to retire from their local business *with the State's consent. Day v. T. R. & R. Co.*, 80 Wash. 161, 166 and cases cited. But neither appellant contends that it has ever sought the State's permission to renounce its local business. Until it does so, it is hardly in a position to claim that such consent, if in fact necessary, would be withheld.

TAX ACT ITSELF PERMITS WITHDRAWAL.

The Act provides:

"If any person shall engage or continue in any business * * * for which a privilege tax is imposed by this act, he shall be deemed to have applied for and to have duly obtained from the State of Washington, a license under this act to engage in and to conduct such business * * * for the current tax year, upon the condition that he shall pay the tax accruing to the State of Washington under the provisions of this act; and he shall hereby be duly licensed to engage in and conduct such business or perform such function." (Sec. 3, ch. 191, Laws of 1933.)

Another section (Sec. 17, ch. 1[illegible], Laws 1933) provides for the institution of injunction proceedings in the name of the state to restrain the continuance of any taxable business until the tax is paid.

Any person or corporation engaged in a taxable activity is thus given the option of either withdrawing therefrom, or paying the tax. Surely the sovereign State exacting such tax could not be heard to complain of such renunciation.

By the very constitutional provisions upon which appellants rely, railroad, telegraph and telephone companies are "declared to be common carriers and *subject to legislative control.*" (See Art. XII, Secs. 13 and 19.) Surely, no form of "legislative control" could be deemed more legitimate than the exercise of the right of taxation. Nor could the prohibition until payment of the continuance of the business taxed, be deemed an unreasonable or unusual method of tax enforcement.

Article 11, Sec. 5, of the Idaho Constitution provides:

"All railroads shall be public highways, and all railroad, transportation, and express companies shall be

common carriers, and *subject to legislative control,*" etc.

The case of *Northern Pacific Ry. Co. v. Gifford,* 25 Ida. 196, 136 Pac. 1131, 1136, involved the validity of a license tax measured by authorized capital stock, imposed upon all foreign and domestic corporations doing a local business in the state of Idaho. In upholding the tax as to foreign railroad and express companies doing an interstate and local business the court said:

"In this connection it has been suggested by counsel for respondent that under the provisions of section 5 of article 11, of the state Constitution the respondent corporation as a common carrier could not decline or refuse to carry on domestic or intrastate business. This provision of the Constitution is dealing with domestic business and with corporations doing business in this state as distinguished from interstate business. *Foore v. Simon Piano Co., supra.* But, if it were otherwise, this provision of the Constitution says they are subject to *legislative control,* and in the case at bar the Legislature has spoken and designated the terms on which respondent can do business in the state, and that, upon failure to comply with the legislative requirement, it shall have no existence or standing in the state so far as local and intrastate business is concerned, and shall have no standing in the courts for the purpose of prosecuting actions or defending any rights of property. *We conclude, therefore, that to refuse to comply with this provision of the statute, and to become outlawed so far as it involves its right to do business in this state, would not subject it to another process compelling it to do the very business that it is prohibited doing under this legislative direction.*" (Italics ours.)

The foregoing decision was later adhered to in *Northern Pacific Ry. Co. v. Gifford,* 27 Ida. 667, 151 Pac. 909.

Here, as in the Idaho case, the legislature has designated the terms on which appellants may do a local business in this state, namely, by paying the occupational tax exacted, and that upon failure so to do, they have no

right to continue a local business. In view of this requirement, it would seem that the conclusion of the Idaho court is inevitable.

In *State v. Northern Express Co.*, 80 Wash. 309, it was held that a state law levying an excise or privilege tax upon express companies measured by 5% of their gross receipts from intrastate business only, did not impose a burden upon interstate commerce.

It was further held that since the State had no power to place a burden upon interstate commerce, an interstate express company doing business in that state was free to renounce its intrastate business, notwithstanding the constitutional and statutory provisions making express companies common carriers subject to state control, and prohibiting discrimination in privileges and transportation charges.

The case was heard *en banc*, the court overruling its former departmental decision (76 Wash. 636) relied upon by appellants here.

Answering the express company's contention that under the state statutes and constitution it was not at liberty to abandon its intrastate business while continuing its interstate activities within the State, the Court said, after reviewing numerous decisions including *Pullman Co. v. Adams*, 189 U. S. 420:

"Respondents make a general reference to the public service commission law of 1911 as supporting their contentions. It may be answered that no provision of that law could operate as a regulation upon interstate commerce. All that it seeks to do, and all that the state has power to do, is to impose regulations upon local business, and while the state cannot say to the foreign corporation, 'We will annex certain conditions with which you must comply before you can do an inter-

state business in or through this state,' it can say to such corporation, 'If you choose to do a business which is purely local in its character and which has attached to it no elements of interstate commerce, you must submit that business to the regulation and control of the laws of this state.' To go further than this, the state has not attempted, or if it has, its attempt is vain. So far as any constitutional provision is concerned, we find no essential difference between our constitution and that of the State of Mississippi referred to in the *Adams* case. Our constitution provides, in Sec. 13, Art. 12, that 'all railroad, canal and other transportation companies are declared to be common carriers and subject to legislative control.' Section 195 of the constitution of Mississippi reads: 'Express, telegraph, telephone, and sleeping car companies are declared common carriers in their respective lines of business, and subject to liability as such.' If, under this provision of the Mississippi constitution, nothing could be found compelling express companies to do a local business, we can find nothing in the language of our constitution which adds any such power. The whole theory of state control of public service corporations is based upon the doctrine, as expressed in *Munn v. Illinois,* 94 U. S. 113, that, when one devotes his property to a public use, he grants to the public an interest in that use, and must submit to be controlled by the public for the public good to the extent of the interest he has created. 'He may withdraw his grant by discontinuing the use, but so long as he maintains the use, he must submit to control.' So here the express company may withdraw its property from any local use and discontinue such use; but so long as it continues in such use, it must submit to state control and regulation.'' (pp. 324-5.)

It will be urged that the *Northern Express* case was modified or overruled in the later case of *Great Northern Railway Co. v. State,* 147 Wash. 630, 646-7, likewise an *en banc* decision, wherein appears the following language:

''We are firmly convinced, however, and we are bound by our convictions to so decide, that under the more recent cases of the supreme court of the United

States, particularly that largely quoted from, *International Paper Co. v. Commonwealth of Massachusetts, supra,* the operation of the statutes in question here, under the commerce clause of the federal constitution, necessarily burdens such interstate commerce, *because (1)of the legal condition that respondent is a public carrier largely engaged in business in this state and not free to withdraw therefrom;* (2) under such conditions the state by the exaction of these fees is compelling such foreign corporation, as a condition of its right to do a local business in this state, to submit to a burden on its interstate business; and, (3) that the statutes violate the due process clause of the Fourteenth Amendment to the federal constitution because of imposing a tax on property beyond the jurisdiction of the state." (Italics ours.)

The court does not say, it is to be noted, whether the company's want of ability to withdraw was due to restrictions in the State or federal statutes, or to practical necessity.

What the court intended to say, we submit, is that the interstate railroad company was not free to withdraw as a practical matter, by reason of the intercommingling of its intra and interstate activities—and for the following reasons:

(1) The court says, it will be noted:

"We are firmly convinced * * * that *under the more recent cases of the supreme court of the United States* * * * the statutes in question * * * necessarily burdens such interstate commerce, because (1) of the legal condition that respondent is a public carrier largely engaged in business in this state and not free to withdraw therefrom;" etc. (Italics ours.)

But a careful search shows that there were no United States supreme court decisions tending to support the conclusion that the railroad company was forbidden by constitution or statute from withdrawing from its local business.

(2) Other language used in the opinion shows that the court could not have intended that the company was forbidden by law from withdrawing from its local business. Thus, in commenting on a case relied upon by counsel, the court said (147 Wash. 646):

"It will be noted that that case was not a case involving a public carrier required to do business in this state and unable to withdraw therefrom. *It was more free to withdraw* than was Northern Express Company in the case cited in 80 Wash. 309, 141 Pac. 757, and perhaps as free to withdraw as the two complaining parties in 136 Wash. 285, 239 Pac. 840 and 138 Wash. 72, 244 Pac. 398, cases heretofore cited." (Italics ours.)

It is apparent, of course, that here the court was speaking of the ability of the company to withdraw from its state business *as a practical matter*. Otherwise, why imply that there were different degrees of freedom to withdraw? If continued operation was made mandatory by constitution or statute, the duty was absolute, not relative.

(3) After having so exhaustively considered the question in the *Northern Express* case (80 Wash. 309), and having concluded that an interstate carrier was under no statutory or constitutional compulsion to continue its intrastate operations, it is inconceivable that the court could have intended, without discussion, to have overruled its earlier decision.

But were there any doubt as to the effect of the Great Northern case on the attitude of the present court, it is, we submit, set at rest by what was said in the cases from which these appeals are taken. To quote:

"So far as the opinion in the case of *Great Northern R. Co. v. State*, 147 Wash. 630, 267 Pac. 506, is out of harmony with the holding in this case, it will be dis-

approved." *State v. N. P. Ry. Co.*, 83 Wash. Dec. 52, 62, 48 Pac. (2d) 931, NP Rec. 54, 63.

IT IS NO LONGER WITHIN THE STATE'S POWER TO DENY THE APPELLANT RAILROADS THE RIGHT TO DISCONTINUE THEIR INTRASTATE ACTIVITIES.

It is, of course, recognized by all courts that Congress has the unquestioned right to regulate intrastate commerce when the situation becomes such, by reason of the interblending of the interstate and intrastate operations of the enterprise that adequate regulation of the particular commerce between the states cannot be maintained without regulating intrastate transactions of a like character.

This rule is elaborately and convincingly explained in the well considered case of *Stafford v. Wallace*, 258 U. S. 495, 517 *et seq.*, where the authorities are cited and reviewed. More recent cases affirming this rule are: *Georgia Public Service Com. v. U. S.*, 283 U. S. 765; *Alabama v. U. S.*, 283 U. S. 776, and *U. S. v. Louisiana*, 290 U. S. 70.

Thus, in *Railroad Commission v. C. B. & Q. R. Co.*, 257 U. S. 563, it was held that the I. C. C. had authority under the Transportation Act of 1920 to fix passenger rates on intrastate business to the end "that intrastate traffic should pay a fair proportionate share of the cost of maintaining an adequate railway system," both intra and interstate.

And in *Colorado v. U. S.*, 271 U. S. 153, it was held that under the 1920 Transportation Act the I. C. C. had power to authorize abandonment, as respects both intrastate and interstate traffic, of a branch line of railroad lying wholly within a state, upon the ground that con-

tinued operation would result in large operating deficits constituting an undue burden upon interstate commerce, even where the State was present resisting such abandonment.

In *Texas v. U. S.*, 292 U. S. 522, it was held that the I. C. C. has power to authorize a lease of one interstate railway to another permitting the lessee to abandon or remove general offices and shops of the lessor, the maintenance of which as found by the Commission would entail unnecessary and wasteful expenditures, even though such abandonment or removal was forbidden by the statutes of the State of the lessor's incorporation in which such offices and shops were located.

"Even explicit charter provisions," it was there said, "must yield to the paramount regulatory power of the Congress."

And Your Honors cited numerous authorities as supporting the following excerpt:

"Obligations assumed by the corporation under its charter of providing intrastate service are subordinate to the performance by it of its federal duty, also assumed, 'efficiently to render transportation services in interstate commerce.'" (292 U. S. 531-2.)

It must therefore follow that whatever provisions may be found in the constitution and statutes of the state of Washington which might be so construed as to impose the absolute duty upon interstate railroads of continuing their intrastate business, such provisions, even if otherwise valid, are now, if not wholly superseded, at least suspended and no longer effective by reason of the field being wholly occupied by paramount federal regulations.

FEDERAL REGULATION DOES NOT PREVENT STATE TAXATION.

But it is equally true that Congress has never undertaken to control the action of the states in the imposition

on interstate carriers of either *ad valorem* or privilege taxes.

In *Federal Compress & Warehouse Co. v. McLean,* 291 U. S. 17, 23, this Court said:

"The mere extension of control over a business by the national government does not withdraw it from a local tax which presents no obstacle to the execution of the national policy."

No such "obstacle" is, we submit, presented where, as heretofore shown, the State's New Tax Plan actually results in a substantial reduction of the carrier's aggregate tax burden.

The tax there involved was a non-discriminatory tax on the business of storing and compressing cotton.

The following is quoted from *Western Union Tel. Co. v. Texas,* 105 U. S. 460, 466:

"The rule that the regulation of commerce which is confined exclusively within the jurisdiction and territory of a state, and does not affect other nations or states or the Indian Tribes, that is to say, the purely internal commerce of a state, belongs exclusively to the state, is as well settled as that the regulation of commerce which does affect other nations or states or the Indian Tribes belongs to Congress. Any tax, therefore, which the state may put on messages sent by private parties, and not by the agents of the government of the United States, from one place to another exclusively within its own jurisdiction, will not be repugnant to the Constitution of the United States."

In *Osborne v. Florida,* 164 U. S. 650, 655, it was said:

"It has never been held * * * that when the business of the company which is wholly within the state, is but a mere incident to its interstate business, such fact would furnish any obstacle to the valid taxation by the state of the business of the company which is entirely local."

(Quoted in *Kehrer v. Stewart*, 197 U. S. 60, 68, and *Allen v. Pullman Car Co.*, 191 U. S. 171, 181.)

"The importance of the commerce clause to the Union," said Mr. Justice Holmes in *Superior Oil Co. v. Mississippi*, 280 U. S. 390, 395, "of course is very great. *But it also is important to prevent that clause being used to deprive the States of their life-blood by a strained interpretation of facts.*" (Italics ours.)

The following language of the supreme court of Mississippi is impressive:

"It does not matter whether the intrastate business done was nearly equal to the interstate business, the state's control over the intrastate business is full and complete, subject only to the provisions of the Federal Constitution. The powers of the state, not given to the United States government by the Federal Constitution, are reserved to the state or the people. The state constitutes an essential unit in the federal scheme, and the state should not be embarrassed in the operation of its functions within its sphere, but should be left to discharge those functions according to its own conception thereof. This nation, as it was founded, cannot exist without the states fulfilling their proper functions in the scheme. The importance of the powers and rights of the states have not been magnified, and have been frequently overlooked. The power of the state is not restricted except by the Federal Constitution or the State Constitution.

"That which is inherent in intrastate commerce does not lose its essential nature when it becomes a part of transactions in interstate commerce. *York Mfg. Co. v. Colley*, 247 U. S. 21. • • •

"The constitutional equality of the states is essential to the harmonious operation of the scheme upon which the republic was organized. This country is an indestructible union of indestructible states. *Coyle v. Smith*, 221 U. S. 559, 31 S. Ct. 688, 55 L. Ed. 853; *White v. Hart et al.*, 13 Wall. (80 U. S.) 646, 20 L. Ed. 685. In *Texas v. White* it was held that, if a state would exercise its sovereign power, then it must be permitted to exercise its legitimate power in all legitimate ways." *Chassanoil v. Greenwood*, 166 Miss. 848, 148 So. 781, 786.

"We must remember," as Your Honors emphasized in *Flint v. Stone Tracy Co.*, 220 U. S. 107, 154, "that the revenues of the United States must be obtained in the same territory, from the same people, and excise taxes must be collected from the same activities, as are also reached by the states in order to support their local government."

Of course the interstate carrier is enabled to enjoy its privilege of engaging in local business primarily as a result of the privilege so to do originally derived from the states themselves. The respective privileges enjoyed by the carrier, derived from the national and state governments respectively, may be likened to two franchises, one from the federal government, and one from the State. Each is a valuable right, taxable by the sovereignty from whom derived, even when such right, having once been exercised, can be abandoned only with the consent of both.

In *Central Pacific R. R. v. California,* 162 U. S. 91, it appeared that the interstate road had two franchises, one from the Federal government and one from the State. The possession of either would have entitled it to operate without the other. The Court sustained the action of the State assessing board in its assessment and taxation of the State franchise notwithstanding the possession by the road of the Federal franchise which was alone sufficient to authorize its operation. In so holding it was said (p. 127):

"If the state franchise to be assessed were confined to the right to operate the road and take tolls, such a franchise was originally granted by the State to this company, and as such was taxable property. If the subsequent acts of Congress had the effect of creating a Federal franchise to operate the road, that merely rendered the state right subordinate to the Federal right, and did not destroy the state right nor merge it into

the Federal right, and no authority is cited to sustain any such proposition. * * * Whether plaintiff in error now operates its road under the franchise derived from the United States or from the state is immaterial, as the Supreme Court well said. The right to operate the road is valuable, whether it is being exercised or not, and the question, we repeat, relates to the existence of the franchise, and not to the extent of its value."

Recognizing the principle that because intrastate activities are not immune from state taxation simply because subject to federal regulation, this court has repeatedly held that decisions holding a given activity subject to state taxation, are not pertinent in determining whether such activity is subject to federal regulation. For example:

"The cases cited by defendants in error, upholding state taxation as not constituting an interference with interstate commerce, are of little value to the inquiry here. It does not follow that because a thing is subject to state taxation it is also immune from Federal regulation under the Commerce Clause. *Stafford v. Wallace, supra,* pp. 525-527; *Addyston Pipe & Steel Co. v. United States,* 175 U. S. 211, 245."

Binderup v. Pathe Exchange, 263 U. S. 291, 311.

Besides the cases cited in the above excerpt, see also *Swift & Co. v. U. S.*, 196 U. S. 375, 400.

STATE IS LIKEWISE WITHOUT POWER TO PREVENT THE APPELLANT TELEPHONE COMPANY FROM RENOUNCING ITS INTRASTATE BUSINESS.

What has been said in this connection with respect to the appellant railroads, applies also with respect to the appellant telephone company. The intra and interstate activities and instrumentalities of this company are, we submit, no less completely interwoven than are those of the railroad appellants.

It must follow that any state law, whether embodied in constitution or statute, which would seek to condition this company's continued operation as an interstate

instrumentality, upon its continuing to carry on its intrastate activities, however unprofitable the latter might become, would be unquestionably obnoxious to the commerce clause.

True, Congress, while having delegated to the Federal Communication Commission the complete regulation of the interstate activities of telephone companies, has not yet given such Commission jurisdiction of local telephone exchange service where regulated by state commissions (USCA Title 47, Ch. 5, Sec. 221 (b)). But this, we submit, is wholly immaterial. Congress unquestionably has this power if and when it seeks to exercise it, just as truly as in the case of interstate railroads. And a State statute requiring continued intrastate operation as a condition to a continuance of interstate operation would quite obviously just as truly violate the commerce clause, whether Congress has or has not undertaken the regulation of the company's intrastate activities.

This leads us to our next point:

STATE CANNOT LAWFULLY CONDITION A PUBLIC SERVICE COMPANY'S RIGHT TO DO AN INTERSTATE BUSINESS, ON ITS CONTINUING TO DO A LOCAL BUSINESS.

State statutes, imposing conditions on corporations precedent to their right to transact business within the state, are ineffectual to prevent transactions constituting interstate commerce.

Thus a state statute requiring certain classes of foreign corporations to file statements is an invalid restriction and burden and unconstitutional as to foreign corporations engaged in interstate commerce. *Buck Stove and Range Co. v. Vickers*, 226 U. S. 205; *Inter-*

nationa Textbook Co. v. Pigg, 217 U. S. 91; *Crutcher v. Kentucky*, 141 U. S. 47, 56, 57.

And, in *Dahnke-Walker Milling Co. v. Bondurant*, 257 U. S. 282, 291, it was said:

"A corporation of one state may go into another, without obtaining the leave or license of the latter, for all the legitimate purposes of such commerce, and any statute of the latter state which obstructs or lays a burden on the exercise of this privilege is void under the commerce clause. *Crutcher v. Kentucky*, 141 U. S. 47, 57; *Western Union Telegraph Co. v. Kansas*, 216 U. S. 1, 27; *International Text-Book Co. v. Pigg*, 217 U. S. 91, 112; *Sioux Remedy Co. v. Cope*, 235 U. S. 197."

It is of course apparent that if a State may not lawfully impose conditions on the right of a corporation to carry on interstate commerce within its territorial limits, it cannot impose conditions on its continuing to carry on its existing interstate business.

Again—a State may not, in imposing conditions upon the privilege of a foreign corporation's doing business in the state, exact from it a waiver of the exercise of its constitutional right to resort to the federal courts, or thereafter withdraw the privilege of doing business because of its exercise of such right, whether waived in advance or not. *Terral v. Burke Const. Co.*, 257 U. S. 529, 532-3.

Conversely, a State cannot lawfully condition a foreign corporation's constitutional right to engage in interstate commerce within its boundaries, upon its doing a local business therein, or thereafter forbid such interstate activities because of such foreign corporation's renouncing a local business already established.

And see also *Michigan Commission v. Duke*, 266 U. S. 570, and *Buck v. Kuykendall*, 267 U. S. 307.

The Constitution of Mississippi, Art. 7, section 195, provides:

"Express, telegraph, telephone, and sleeping-car companies are declared common carriers in their respective lines of business, and subject to liability as such."

Mississippi Code 1892, Sec. 3378, imposed a privilege tax on each sleeping and palace car company carrying passengers from one point to another in the state of "$100, and, in addition thereto, 25 cents a mile for each mile of railroad over which the company runs its cars."

In *Pullman Co. v. Adams*, 78 Miss. 814, 30 So. 757, it was held no defense to a suit for such taxes, that the local business of defendant, an interstate and intrastate sleeping car company, was done at a loss, and that it could not have declined the business, because, by the above constitutional provision, it was made a common carrier. The court said:

"The contention that the appellant does its local business at a loss, and yet must do it under the constitution of 1890 making it a common carrier, and hence that its interstate business is indirectly burdened, is fallacious. Were that so, it would be the provisions of law declaring the sleeping car companies, common carriers, that would contravene the interstate commerce clause of the federal constitution, not this license tax.

"It is not for the appellant to get all out of the local business the 'traffic will bear' and then escape the correlative burden of this license tax by pleading that it, though conforming to the law making it a common carrier, as to profits, should not conform to the law taxing the business it does wholly local and entirely within this state."

The Mississippi decision was affirmed by the United States Supreme Court in *Pullman Co. v. Adams*, 189 U. S. 420, on the assumption that interstate sleeping car

companies would be held free by the state court to abandon the local business taxed if they saw fit, and in so holding, said:

"If the clause of the state constitution referred to were held to impose the obligation supposed and to be valid, we assume without discussion that the tax would be invalid. For then it would seem to be true that the state constitution and the statute combined would impose a burden on commerce between the states analogous to that which was held bad in *Crutcher v. Kentucky,* 141 U. S. 47. On the other hand, if the Pullman Company, whether called a common carrier or not, had the right to choose between what points it would carry, and therefore to give up the carriage of passengers from one point to another within the state, the case is governed by *Osborne v. Florida;* 164 U. S. 650. The company cannot complain of being taxed for the privilege of doing a local business which it is free to renounce. Both parties agree that the tax is a privilege tax.

"* * * If the constitution of Mississippi should be read as imposing an obligation to take local passengers, the question for us might be which, if not both, the clause of the constitution or the tax act, is invalid. But we assume that the opinion of the Supreme Court of Mississippi intends to meet the difficulty frankly, and when it says that the argument against the tax drawn from the above interpretation of the constitution is fallacious, we take it as meaning that no such interpretation will be attempted in the future, *and we take it so the more readily that we can see no ground for a different view.*" (Italics ours.)

Thus, not only did Your Honors conclude that under the decision of the Mississippi court interstate common carriers are free, if they choose, to renounce their local business while continuing their interstate activities, but expressly say that it "*can see no ground for a different view.*"

The State supreme court took the same view in *State*

v. Northern Express Co., 80 Wash. 309, 324-5, where it was said:

"It is equally fallacious if it is meant by this assertion that, as a condition for engaging in interstate commerce, the state requires the corporation to also engage in intrastate commerce. Such a plea violates a rule concerning which there is now no dispute, that the state can impose no burden upon interstate commerce nor exact any condition upon which foreign corporations may engage in such business within this state. If the constitution should be read as imposing an obligation upon corporations doing an interstate business to also engage in a local business, then, as said in the *Adams* case, 'the question for us might be which, if not both, the clause of the constitution or the tax act, is invalid.'

"Respondents make a general reference to the public service commission law of 1911 as supporting their contentions. It may be answered that no provision of that law could operate as a regulation upon interstate commerce. All that it seeks to do, and all that the state has power to do, is to impose regulations upon local business, and while the state cannot say to the foreign corporation, 'We will annex certain conditions with which you must comply before you can do an interstate business in or through this state,' it can say to such corporation, 'If you choose to do business which is purely local in its character and which has attached to it no elements of interstate commerce, you must submit that business to the regulation and control of the laws of this state.' To go further than this, the state has not attempted, or if it has, its attempt is vain."

Answering a similar contention made by the complaining interstate railroad companies, Judge Neterer said, in *Chicago, M., St. P. & P. R. Co. v. Hedges*, 5 Fed. Supp. 752, 758:

"The contention that the law must fail for that intra and inter state business of the complainants is so inseparably interwoven that interstate (intrastate) business cannot be renounced, is not convincing. Equity does not require a useless thing. The complainants would not renounce intrastate business, which is: N. P., $6,613,-

958.98; interstate, $6,231,366.63. O-W., intrastate, $779,-676.88; interstate, $3,026,256.60. Milwaukee, intrastate, $1,171,236.56; interstate, $2,163,054.27. G. N., intrastate, $1,860,608; interstate, $2,616,837. S. C. P., intrastate, $81,568.98; interstate, $1,333,410.73. Such claim, in the face of the history and record in the case, is fallible. *Ohio Tax Cases,* 232 U. S. 576, 34 S. Ct. 372, 58 L. Ed. 737; *Gant v. Oklahoma City, supra.* While these cases are not directly in point, they are lucid and bear upon the history in the instant issue. Complainants' claim is narrow and without equity, and does not weigh upon conscience. No attempt has been made to renounce, nor purpose to do so, and, until this is done, complainants cannot complain. No right is withheld or denied. The laws and constitution of the state give way to the commerce clause of the United States Constitution (Art. 1, Sec. 8, cl. 3), and the vitalizing Commerce Act (49 USCA-Sec. 1 *et seq.*). See *Colorado v. United States,* 271 U. S. 153, 46 S. Ct. 452, 70 L. Ed. 878. And the rate-making body could and would afford relief, and, if denied, complaint might be available."

That the P. T.'s interstate business is negligible compared with its local business, is shown by the following figures taken from its returns to the tax commission for the last five months of 1933. (Plff's Ex. "22" PT Rec. 131-150):

	Pacific Company
Gross revenues from local and interstate business.....	$4,175,350
Gross revenues from interstate and foreign commerce..	355,662
Percentage of gross revenues from interstate and foreign commerce of total gross revenues within the State.	8.52%

Thus, the language of Judge Neterer is particularly pertinent to that company.

APPELLANTS MAY WITHDRAW FROM LOCAL BUSINESS IF NOT MAKING A FAIR RETURN.

The appellant Telephone Company alleges that for the first six months of 1933 its net earnings on intrastate business were not in excess of 1.75% of the fair value of the property used and useful in furnishing such service.

(PT Rec. 4.) And the N. P. and G. N. each contend that in 1933 it lost money on its intrastate business.

If this be true, then each complaining company has the undoubted right to withdraw from its local business, since the state would certainly not be in a position to compel operation at less than a fair return. But, having voluntarily continued their local operations, they cannot now be heard to claim exoneration from the business tax imposed.

To repeat what was said in *Pullman Co. v. Adams*, 78 Miss. 814, 30 So. 757 (affirmed: 189 U. S. 420):

"It is not for the appellant to get all out of the local business the 'traffic will bear' and then escape the correlative burden of this license tax by pleading that it, though conforming to the law making it a common carrier, as to profits, should not conform to the law taxing the business it does wholly local and entirely within this state."

In this connection, may we observe that the payment of the offending tax is not made a condition precedent to the carrying on of the business upon which the same is imposed. Thus as already noted, section 3, chapter 191, Laws of Washington, 1933, provides:

"If any person shall engage or continue in any business * * * for which a privilege tax is imposed by this act, he shall be deemed to have applied for and to have duly obtained from the State of Washington a license under this act to engage in and to conduct such business or perform such function for the current tax year, upon the condition that he shall pay the tax accruing to the State of Washington under the provisions of this act; and he shall hereby be duly licensed to engage in and conduct such business or perform such a function."

In other words, it is not made unlawful for a person to engage in a taxable business without having first

secured a license. Failure to pay the tax is not made a criminal offense. But if a person continued in the taxable activity after August 1, 1933, he became subject to the tax which could be collected either summarily or by an action at law. (See Sec. 16, ch. 191, Laws 1933.)

That even a domestic corporation may renounce its unprofitable local business though its operations be controlled by regulatory measures similar to those upon which appellants here rely, has been definitely settled by this court.

Thus in *Railroad Commission v. Eastern Texas R. R.*, 264 U. S. 79, it was held that the usual permissive charter of a domestic railroad company did not obligate the company to operate its railroad at a loss, nor was such obligation to be implied from the acceptance of its charter and operation thereunder. In so holding, Your Honors said:

"The company, although devoting its property to the use of the public, does not do so irrevocably or absolutely, but on condition that the public shall supply sufficient traffic on a reasonable rate basis to yield a fair return."

There the Texas statutes relating to railroads were carefully analyzed, from which analysis it was found that they were all of the usual permissive type which did not obligate the company to continue to operate indefinitely.

What was said in that case as to the Texas regulatory statutes applies, we submit, with equal force to all of the numerous statutes and constitutional provisions cited in appellants' briefs and pleadings. *State v. Northern Express Co.*, 80 Wash. 309, 325.

In *I. C. C. v. Oregon-Wash. R. Co.*, 288 U. S. 14, it was held that because the charter of a railroad company authorized it so to do, it was not made its duty to construct and operate an extension to its existing lines.

From the cases cited it seems that a railroad company is under no compulsion to construct a line for the rendition of either interstate or intrastate service even though its charter contemplates such construction and service. Having constructed such line and finding the local business unprofitable, it may abandon such service. Under such circumstances can it be said that there is any contractual obligation to continue operations whether its operations be profitable or unprofitable? We submit not. If there be a contract obligation to operate, it must necessarily exist whether or not its operations prove remunerative.

In this connection, attention is also called to *Williams v. Mayor*, 289 U. S. 36, involving the right of the state of Maryland to grant an exemption from *ad valorem* taxes to a railroad corporation for a period of two years. The railroad was already in operation, and had there been a contract obligation on its part to continue operation, the grant of a tax exemption would, of course, have been without consideration and void. But in upholding the right of the company to such exemption, the court said in part (pp. 44-5):

"It is idle to say that a railroad, when once it has been organized, is under a duty to go on, and hence that its distress is not important for any one except itself. Science has wrought her wonders, but the time is not yet here when trains will run under the impulsion of duty without more. There is room, indeed, for question whether even the duty is so absolute as the respondents' argument assumes. *Railroad Commission v. Eastern Texas R. Co.*, 264 U. S. 79, 85. Certain it is, in any

event, that operation may end with the consent of the Public Service Commission when the earnings are inadequate."

CORPORATION SUBJECT TO PRIVILEGE TAX THOUGH FRANCHISE REQUIRES CONTINUATION OF SERVICE.

That any provisions of the constitution or statutes claimed to impose upon public service companies the continuing duty to operate must be construed in the light of the state's paramount power of taxation, is, we submit, well illustrated by those cases upholding the right of a municipality to impose license taxes upon public service companies operating under an unexpired franchise from the very municipality exacting the tax.

It is of course well established that where a municipal ordinance or state law grants to a public service corporation the right, for the benefit of its inhabitants, to occupy the streets of a city with mains and pipes for furnishing water or gas, wires and poles for lighting or telephone service, or tracks for street car service, and such franchise is accepted and acted upon, the same cannot be revoked by the state or municipality during the life of such franchise. *Northern Ohio Traction & Light Co. v. Ohio*, 245 U. S. 574, 585; *Old Colony Trust Co. v. Omaha*, 230 U. S. 100, 117; *Owensboro v. Cumberland Telephone Co.*, 230 U. S. 58, 73; *Grand Trunk Western Ry. Co. v. South Bend*, 227 U. S. 544, 556; *Louisville v. Cumberland Tel. Co.*, 224 U. S. 649, 664.

It is equally true that when such a franchise has been accepted by the grantee, the same becomes a contract binding the public service company to furnish public service on the terms and conditions set forth in, and *during the life of the franchise. Columbus Ry. & Power Co. v. Columbus*, 249 U. S. 399; *Cleveland v.*

Cleveland City Ry. Co., 194 U. S. 517; *Opelika v. Opelika Sewer Co.*, 265 U. S. 215; *St. Cloud Public Service Co. v. St. Cloud*, 265 U. S. 352; *Henderson Water Co. v. Corporation Com.*, 269 U. S. 278; *Thomas v. Railroad Co.*, 101 U. S. 71, 83; *Gibbs v. Baltimore Gas Co.*, 130 U. S. 396; *Russell v. Sebastian*, 233 U. S. 195, 209.

But notwithstanding such contract obligation assumed by the public service company to continue its public utility operations during the life of its franchise, and the reciprocal obligations of the state or municipality, it is well-recognized that the municipality may nevertheless exact from such public utility company a license tax for the privilege of so performing its franchise obligations.

Memphis Gas Light Co. v. Shelby County, 109 U. S. 398;

Erie Railroad Co. v. Pennsylvania, 21 Wall. 492;

Railway Co. v. Philadelphia, 101 U. S. 528;

St. Louis v. United Railways Co., 210 U. S. 266;

Puget Sound P. & L. Co. v. Seattle, 291 U. S. 619, 627.

In the case last cited it was said:

"Appellant asserts a contract under its franchise to use the streets of the city for the purpose of carrying on its business for an unexpired term of years. It argues that the franchise is a contract license to carry on the business, and that the exaction of a tax as a condition precedent to the enjoyment of the license will operate to destroy the privilege granted by the franchise. This argument was made and answered in *Memphis Gas Co. v. Shelby County*, 109 U. S. 398, and in *St. Louis v. United Railways Co.*, 210 U. S. 266. Surrender of the state's power to tax the privilege is not to be implied from the grant of it. Hence, appellant took its franchise subject to the power of the state to tax the granted privilege in common with all other privileges

and property in the state. Without a clearly expressed obligation on the part of the city to surrender that power the contract clause does not limit it." (Citing authorities.)

None of the appellants either alleged or proved when they began to do an intrastate business within the state of Washington. As a matter of fact it was in each case, long after the adoption of the State constitution in 1889. Hence, if the obligations imposed by the state constitution be likened to the contract obligations assumed by the Puget Sound Light & Power Company in the case last cited, then obviously such obligations were assumed with full knowledge of the State's right to impose the tax now complained of just as the Puget Sound Company did in that case.

Every presumption is in favor of the reservation by the State of the complete exercise of its fundamental right to tax. *Tacoma v. State Tax Commission,* 177 Wash. 604, 611.

We respectfully submit that this presumption obtains just as truly to constitutional provisions as to statutes. By simply imposing upon certain corporations the obligations of public service companies, the constitutional convention did not, we insist, evidence an intent to relieve such corporations from taxation for the privilege of so functioning. Instead, a contrary purpose is evidenced by section 1, article 12, of the State constitution, providing that "all laws relating to corporations may be altered, amended, or repealed by the legislature at any time," and that "all corporations doing business in this state may, as to such business, be regulated, limited, or restrained by law." Surely, conditioning the right to continue operations upon the payment of a legiti-

mate occupational tax does violence neither to this section nor to the right of "legislative control" reserved as to these public service companies. (See Art. 12, Sec. 13, 19 Wash. St. Const.)

CONTENTION THAT SAME INSTRUMENTALITIES ARE USED IN BOTH INTRA AND INTERSTATE BUSINESS, AND RENUNCIATION OF INTRASTATE BUSINESS WOULD RESULT IN INTERSTATE RATES GREATER THAN TRAFFIC COULD BEAR.

The P. T. alleges that its interstate and intrastate business is done over the same lines, through the same exchanges, by the same employees, and with the same facilities, and that it is impossible for it to operate otherwise, and that if it could and should abandon its intrastate business, the entire burden of maintaining and operating its intrastate system, equipped to handle both classes of business, would fall entirely on interstate business and would necessitate an increase of rates greater than the same could bear and would result in the destruction of an essential instrument of interstate commerce and of the value of its properties in amounts of many millions of dollars. (PT Rec. 5-6.)

The answers of the appellant railroads contain similar allegations. (NP Rec. 10-11; GN Rec. 17-19.)

Whether or not these averments are supported by the evidence is discussed in Appendix "C," Post, pp. 181-7.

But even accepting such allegations at their face value, this, we submit, would be no defense to a business tax measured solely by a percentage of their intrastate revenues.

May we first point out that appellants constructed

their properties fully conscious of the State's undoubted right to impose excises on their intrastate business. They need not renounce such local business so long as they pay the tax. It is not shown, as we have seen, that, by adjustment of intrastate rates, the offending tax cannot be passed on to appellants' customers. Their election to withdraw from intrastate business will, if made, be purely voluntary.

Obviously the same objection here advanced might be made with equal plausibility to any duty imposed on appellants in connection with their intrastate business, whether it be the payment of a license tax or compliance with some rule or order of the state regulatory body. Let us suppose that the D. P. W. should promulgate some (to appellants) offensive rule or regulation affecting telephone or railroad intrastate operations. Could appellants be heard to question the validity of such regulation on the ground that the expense of carrying on their interstate business would be increased by the abandonment of their intrastate business thereby necessitating an increase of interstate rates and a consequent burden on interstate commerce?

Were appellants' operations confined wholly to intrastate business, the validity of the occupation tax as applied to these objecting companies could not be questioned. Because these companies are also engaged in interstate business, this tax which is imposed only on their intrastate receipts and which is not in the slightest degree increased by their interstate operations cannot, we submit, be said to constitute an unlawful burden on interstate commerce. The possible indirect effect on their interstate business visioned by appellants is, we

submit, too remote and fanciful to be deemed a valid objection to the tax.

While the states are without power directly to regulate, prohibit, or burden interstate commerce, yet, to come within the rule, such interference must be direct and substantial, and not merely incidental. The states may, so long as they do no more than legitimately exercise their reserved police and taxing power, enact laws which will be valid, although they may incidentally affect interstate commerce. 12 C. J. 13, 50; *Boston & Maine R. Co. v. Armburg,* 285 U. S. 234, 238, and cases cited.

The length to which this court has gone in upholding state legislation potentially but not directly affecting interstate commerce is, we submit, illustrated by its early decisions in *Reading R. Co. v. Pennsylvania,* 15 Wall. 284, and *State of Maine v. Grand Trunk Ry. Co.,* 142 U. S. 217, upholding state excise taxes measured by the gross receipts of foreign and domestic railway companies derived from both their intra and interstate business.

And while, as heretofore shown, Your Honors, in *Galveston, Harrisburg etc. Ry. Co. v. Texas,* 210 U. S. 217, in a five-to-four decision, held invalid a Texas statute of this kind, so far as interstate revenues were concerned, never, so far as we can find, has this court held a state occupational tax, measured only by the intrastate gross receipts of interstate public service companies, whether foreign or domestic, unconstitutional as violative of the commerce clause.

Were it true, as claimed, that appellants' intra and interstate businesses are hopelessly commingled we may

assume that a state excise imposed directly upon their instrumentalities used in both activities, such as cars, engines, or telephone instruments, would offend the commerce clause.

But this, if the court pleases, is not true of *a tax measured by a percentage of gross receipts from intrastate business only.* Such a tax cannot, we submit, be held to burden appellants' interstate operations. Appellants' instrumentalities used in interstate operations are taxed only to the extent that the same are used in local service. If not so used, they are not taxed at all.

We know of no decision, and are confident counsel can cite none, striking down an occupational tax measured only by intrastate revenues, however intercommingled may be the local and interstate operations of the public service company. On the other hand, such a tax has been in numerous cases sustained by this court.

It is a matter of common knowledge, of course, that the instrumentalities of railroads and telegraph companies in carrying on their intra and interstate activities are no less commingled than are those of interstate telephone companies. To possibly a lesser extent this is likewise true of express and sleeping car companies.

In *Pacific Express Co. v. Seibert,* 142 U. S. 339, a privilege tax measured by 2% of the interstate express company's local revenues was sustained. On the other hand, in the later case of *Barrett v. New York,* 232 U. S. 14, a city ordinance imposing a license tax *directly on an interstate express company's express wagons* used in hauling both interstate and local express was condemned as a burden on interstate commerce.

We may add that in *Osborne v. Florida,* 164 U. S. 650, a lump-sum license tax imposed by cities upon ex-

press companies doing both intra and interstate business was sustained.

In *Pullman Co. v. Adams,* 189 U. S. 420, an excise measured in part by the mileage of line operated by a sleeping car company doing both local and interstate business was sustained. A lump sum excise tax was sustained as to a company doing the same kind of business in *Allen v. Pullman Co.,* 191 U. S. 171.

In *Western Union Tel. Co. v. Alabama,* 132 U. S. 472, and *Ratterman v. Western Union Tel. Co.,* 127 U. S. 411, occupational taxes measured by a percentage of local revenues were sustained as to telegraph companies doing both a local and interstate business, while in *Telegraph Co. v. Texas,* 105 U. S. 460, an excise measured by the number of intrastate messages sent, was sustained as to an interstate company.

And in *Postal Tel.-Cable Co. v. Fremont,* 255 U. S. 124, *Postal Tel.-Cable Co. v. Richmond,* 249 U. S. 252, and *Postal Tel.-Cable Co. v. Charleston,* 153 U. S. 692, lump sum license taxes imposed by municipalities on interstate telegraph companies for the privilege of doing a local business were sustained.

In *Lehigh Valley R. Co. v. Pennsylvania,* 145 U. S. 192, and the well-considered case of *Ohio River & W. R. Co. v. Dittey,* 232 U. S. 576 (the "Ohio Tax Cases"), occupational taxes measured by a percentage of local revenue, were sustained as to railroad companies doing both intra and interstate business.

In *St. Louis S. Ry. Co. v. Arkansas ex rel. Norwood,* 235 U. S. 350, a privilege tax measured by the proportion of the company's capital stock used within the state,

was sustained as to a foreign railway company doing both intra and interstate business.

In *People ex rel. Cornell Steamboat Co. v. Sohmer*, 235 U. S. 549, a privilege tax measured by local gross earnings was sustained as to a navigation company doing both local and interstate business.

Is it not, we ask, most remarkable that if counsel's position be sound, the same would not have been successfully urged in some one of these numerous cases?

Were counsel's contention meritorious, no good reason could, we submit, be suggested why the tax should not for the same reason be condemned as to every private enterprise compelled by economic necessity to use the same instrumentalities in doing both a local and interstate business. Yet who would seriously urge that such institutions as Sears-Roebuck or Montgomery Ward should be relieved from the tax on this ground?

Indeed, this court has held directly contrary to appellants' contention.

In *Bowman v. Continental Oil Co.*, 256 U. S. 642, a statute of New Mexico, applicable to distributors of gasoline, imposed an excise of two cents for each gallon sold or used, and an annual license tax of $50.00, payable in advance, for each distributing station, place of business or agency. The law was held invalid as to the $50.00 license tax *on each distributing station* as a direct tax on an interstate instrumentality, the court saying (p. 648):

"No doubt the State might impose a license tax upon the distribution and sale of gasoline in domestic commerce if it did not make its payment a condition of carrying on interstate or foreign commerce. But the State has not done this by any act of legislation. * * *

But the difficulty is that, since *plaintiff, so far as appears, necessarily conducts its interstate and domestic commerce in gasoline indiscriminately at the same stations and by the same agencies, the license tax cannot be enforced at all without interfering with interstate commerce.* * * *." (Italics ours.)

Thus, in the *Bowman* case the contestant established precisely the same defense asserted here, namely, that it necessarily conducted its interstate and domestic commerce in gasoline at the same stations and by the same agencies. Yet this court upheld that part of the law imposing a 2 cent gallonage tax on gasoline in so far as it applied to domestic sales, Your Honors saying (p. 646):

"* * * so far as the excise tax is concerned—imposed as it is upon the sale and use of gasoline according to the number of gallons sold and used—the divisible nature of the subject renders it feasible to control the operation and effect of the tax so as to prevent it from being imposed upon sales in interstate commerce, while allowing the State to enforce it with respect to domestic transactions and with the allowance of an injunction limited accordingly plaintiff will receive the full protection to which it is entitled under the Constitution of the United States."

Examination will show that in all of the cases relied upon by appellants, the tax was imposed on *the interstate instrumentality itself,* and not merely measured by intrastate revenues from such instrumentality, as shown by the following review:

Interstate Busses v. Holyoke Street Ry., 273 U. S. 45:

There the state law complained of by the carrier operating an interstate and intrastate bus line required a license of *all* for-hire motor vehicles and also a certificate of public convenience and necessity issued by the state regulatory body. Neither license nor certificate

were required as to carriage exclusively interstate. The carrier contended that since it carried both interstate and local passengers on the same busses, the state regulation was invalid and unenforcible as to it, as a burden on interstate commerce. But the court said (p. 51):

"It is not shown that the two classes of business are so commingled that the separation of one from the other is not reasonably practicable or that appellant's interstate passengers may not be carried efficiently and economically in busses used exclusively for that purpose or that appellant's interstate business is dependent in any degree upon the local business in question. Appellant may not evade the Act by the mere linking of its intrastate transportation to its interstate or by the unnecessary transportation of both classes by means of the same instrumentalities and employes."

Now, let us assume that the court had there actually found that the bus company was in fact compelled by unavoidable circumstances to use the same busses for the carriage of both interstate and local passengers, and for that reason had held the state law invalid as a burden on interstate commerce, would this case, even on this assumption, lend color to counsel's contention? Obviously not, for the reason that such statutory requirement of a license and certificate of necessity would then have been a *direct burden* on the carrier's interstate business—a regulation of the *instrumentalities themselves,* used by the carrier in its interstate operations. The issuance of licenses and granting of a certificate of necessity being within the discretion of the state officers, the extent of the service rendered would likewise obviously be within the control of such authorities. Such a law, it might plausibly be argued, would directly burden and restrict interstate commerce.

On the contrary, the Washington Occupational Tax

Act in no way interferes with appellants' interstate operations. These companies may carry on their interstate business as they see fit, and are limited in their local operations only to the extent that they must contribute to the support of the state government for the privilege of so doing. Surely, this is not a *direct* burden on interstate commerce forbidden by the commerce clause.

LeLoup v. Port of Mobile, 127 U. S. 640:

In that case the offending city ordinance exacted a license tax from telegraph companies doing business within the city, of $225 per year. The ordinance was applicable to all companies whether engaged in intrastate or interstate business, or both, and imposed a fine for failure to pay the license fee imposed. The court said as to the point involved:

"The question is squarely presented to us, therefore, whether a state, as a condition of doing business within its jurisdiction, may exact a license tax from a telegraph company, a large part of whose business is the transmission of messages from one state to another and between the United States and foreign countries * * *. We are not prepared to say that this can be done."

There, the burden on interstate commerce was more direct even than had the tax been directly imposed on the interstate instrumentality. It was exacted of the interstate telegraph company itself.

It is interesting to note that in that case the companies were paying in addition to a property tax, "a tax of three-quarters of one per cent on their gross receipts within the state." (p. 645.) *As to this occupational tax, no question was raised.*

Western Union Tel. Co. v. Kansas, 216 U. S. 1:

There the offending law required that the telegraph company pay a given percentage of its authorized capital, whenever and however employed, as a condition to its right to continue to do domestic business in Kansas. It was held that such a tax burdened interstate commerce and taxed property beyond the limits of the State.

It thus appears that the tax here assailed is in no way similar to that imposed under the Kansas law.

Postal Tel.-Cable Co. v. Richmond, 249 U. S. 252:

There a license tax imposed on intrastate business was upheld as against the objection that it imposed a burden on the company's interstate business because the net receipts from its intrastate business were insufficient to pay the tax, and the payment would therefore have to be made from inferstate receipts.

Barrett v. New York, 232 U. S. 14:

There an ordinance of the city of New York imposed a license fee, not upon or measured by the intrastate revenues of the express company, but upon the *very instrumentality* used in its interstate business, namely, the express wagons used to haul both kinds of business.

Bowman v. Continental Oil Co., 256 U. S. 642:

The tax there held bad was a license tax of $50 per station imposed on companies distributing gasoline in both domestic and interstate commerce. It was shown that the company necessarily conducted its interstate and domestic commerce in gasoline indiscriminately at the same stations and by the same agencies. It was held under those circumstances that the tax was void as a burden on interstate commerce. There again, the tax

was on the interstate instrumentality itself, the gasoline station.

As already noted, this case is a highly presuasive authority in support of the tax here in question.

The distinction between this class of cases and the case at bar is, we submit, clearly pointed out in the recent case of *Cooney v. Mountain States Tel. & Tel. Co.*, — U. S. —, 55 Sup. Ct. 477, 482, 79 L. Ed. 498, 504, where Your Honors said as to a privilege tax made applicable to telephone instruments used in both interstate and intrastate business:

"A privilege or occupation tax which a State imposes with respect to both interstate and intrastate business, through an indiscriminate application to instrumentalities common to both sorts of commerce, has frequently been held to be invalid. • • • *Barrett v. New York*, 232 U. S. 14, 29, 31. • • • *Bowman v. Continental Oil Co.*, 256 U. S. 642, 647, 648, 65 L. Ed. 1130, 1144, 1145, 41 S. Ct. 606. In the cases of the express companies, the principle was applied to a privilege tax imposed alike with respect to wagons used in the movement of both interstate and intrastate shipments. The local shipments 'were handled in the same vehicles, and by the same men' that were employed in connection with the interstate transportation and it was impracticable to effect a separation. *Barrett v. New York*, 232 U. S. 14, 58 L. Ed. 483, 34 S. Ct. 203, and *Platt v. New York*, 232 U. S. 35, 58 L. Ed. 492, 34 S. Ct. 209, *supra*. In *Bowman v. Continental Oil Co.*, 256 U. S. 642, 65 L. Ed. 1139, 41 S. Ct. 606, supra, the question arose under a statute of New Mexico laying an annual license tax of five dollars for each station distributing gasoline. The court pointed out the distinction between an excise tax on sales of gasoline where, as the subject matter was separable, full protection could be afforded by enjoining enforcement as to the interstate business, and the license tax which with its prohibition fell upon the business as a whole. The Court said: 'But with the license tax it is otherwise. If the statute is inseparable, then both by its terms and by its legal operation and effect

this tax is imposed generally upon the entire business conducted, including interstate commerce as well as domestic; and the tax is void.' The difficulty, continued the Court, 'is that, since plaintiff, so far as appears, necessarily conducts its interstate and domestic commerce in gasoline indiscriminately at the same stations and by the same agencies, the license tax cannot be enforced at all without interfering with interstate commerce unless it be enforced otherwise than as prescribed by the statute—that is to say, without authority of law. Hence, it cannot be enforced at all.'

"In the instant case, the tax, being indivisible and indiscriminate in its application, necessarily burdens interstate commerce."

Although we have reviewed only those cases relied upon by appellants' counsel, we are satisfied that all cases in which state or municipal regulatory or tax measures have been held repugnant to the commerce clause are readily distinguishable for the same reason pointed out with respect to the *Holyoke* and *Adams Express* cases. And in no case decided by the highest court, has a state excise tax or ordinance been adjudged offensive to the commerce clause, where imposed for the privilege of doing, and measured by gross income from, interstate business alone.

For the reasons urged, we respectfully submit that the judgments of the State supreme court should in each instance be affirmed.

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APPENDIX "A"

Challenge to Trial Court's Findings of Fact and rulings on admissibility of evidence in N. P. Ry. Co. v. State, No. 529.

ASSIGNMENTS NP-3 TO NP-33

Each railroad appellant owns and operates a railroad between Puget Sound and the Great Lakes. As such interstate carrier, each keeps its system accounts as prescribed by the I. C. C. (GN Rec. 110, NP Rec. 79.) The I. C. C., however, does not prescribe rules for the apportionment of system revenues and expenses as between the various states through which such appellants operate. (GN Rec. 110.)

Whether each road's local business is profitable or unprofitable depends, of course, upon the amount of its intrastate revenues less operating expenses and taxes properly chargeable to its intrastate operations.

Such local revenues can obviously be ascertained with reasonable accuracy. But where, as here, these companies' local traffic is handled at the same terminals, and hauled over the same rails, on the same trains, by the same engines, and with the same employes, as their interstate traffic, the extreme difficulty of accurately apportioning these joint operating expenses to local traffic becomes at once apparent. Consequently, any method or methods proposed for so doing, must, we submit, be scrutinized with the utmost caution before the court can set aside a revenue measure on the theory

that the railroad so taxed is in fact losing money on its local business.

It must be remembered that these roads do both an intra and interstate passenger business, and an intra and interstate freight business over the same rails. Consequently, to discover what proportion of their operating expenses should equitably be apportioned to their intrastate traffic, these roads were confronted, among numerous others, with the following problems:

(1) The apportionment of system operating expenses as between freight and passenger service;

(2) The apportionment of each of some hundreds of different items of system passenger expenses and system freight expenses to its Washington operations;

(3) The apportionment of each of these numerous items of passenger and freight expenses (so apportioned to Washington) as between Washington intra and interstate freight and passenger service.

Pursuant to the I. C. C.'s instructions, each railroad divides its system operating expenses under some 197 separate and distinct accounts, and in reporting its operating expenses in Washington to the D. P. W., each company uses these same accounts and account numbers. (See NP Ex. "9," pp. 702-707, NP Rec. 276-281.) These accounts are divided into the following six main divisions of operating expenses:

(1) "Maintenance of Way and Structures"; (2) "Maintenance of Equipment"; (3) "Traffic"; (4) "Transportation — Rail Line"; (5) "Miscellaneous Operations" (which includes such items as dining and buffet service, hotels and restaurants, grain elevators,

stockyards, etc.); and (6) "General" (which includes salaries of officers and clerks, legal expenses, etc.).

Confronted with the problem of isolating its operating expenses incident to local traffic, each road pursued the following course:

It proceeded on the assumption, first, that its operating expenses incident to its operations, both intra and interstate, in the state of Washington, were, as to both freight and passenger traffic, accurately shown in its reports to the D. P. W. for 1933 and previous years.

All intra and interstate passenger service expense as so reported was apportioned as between intra and interstate passenger service (a) by the N. P. according to relative intra and interstate passenger miles (a method challenged by the State); and (b) by the G. N., according to the relative intra and interstate passenger revenue (a method not contested by the State).

But the segregation of intrastate freight service expenses did not prove so simple. Intra and interstate freight, it was found, was hauled (as above noted) over the same rails, by the same engines, in the same cars and trains, by the same employes, and by means of the same terminal facilities. Moreover, freight movements were found to involve at least two distinct classes of expenses: (1) line-haul expense and (2) terminal expense. Each road, therefore, undertook to make two special studies each covering a seven-day period—one to determine the average cost of the various elements of terminal or switching expense, and the other to ascertain the line-haul expense incident to local freight traffic. Having purported to find the total line-haul expense for the test week chosen, and the number and character of

the various switching operations incident thereto, and having, in a separate study, purported to find the cost of such various switching operations, it purported to calculate therefrom the total operating expenses incident to the intrastate operations for the test week. The total operating expenses incident to intrastate freight traffic for 1933 were then computed by the two roads in substantially the following manner: As to the N. P., the cost per intrastate revenue ton mile was found for the week, and such cost multiplied by the total intrastate revenue ton miles for the year. The G. N.'s method was somewhat more complicated, but substantially the same in principle.

To the intrastate freight service operating expenses as so computed, each company then added certain other items of claimed expense (questioned by the State), and thus arrived at what each claimed to be its total intrastate operating expenses for 1933. This amount was then deducted from its claimed total operating revenues for the year (a figure likewise contested by the State), and reached what was termed its "net revenue from railway operations." From the latter figure, each road then deducted what it claimed to be the amount of its 1933 taxes properly apportionable to its intrastate operations. To arrive at this amount, each road apportioned its property taxes as between its intra and interstate traffic in the relation which its intrastate revenues bore to Washington's mileage proportion of its revenues from interstate traffic (a method most vigorously challenged by the State).

The figure arrived at by such deduction of taxes and railway operating expenses from its railway operat-

ing revenues is known as "Railway operating income," and it is this figure which the N. P. claims to be determinative of whether the company has made or lost money for the year. (NP Rec. 97.)

The G. N. contended, however, that for the purpose of determining whether it was doing business at a loss, it was entitled to make the following additional deductions: (1) the excess of rental paid and rental received for the use of equipment ("equipment rentals"); and (2) the excess of rentals paid for the use of tracks and other facilities of other carriers over the rentals received for its own facilities from other carriers ("joint facility rent").

These joint facility rents were apportioned by the G. N. to intrastate traffic in the relation which it found all its operating expenses incident to intrastate traffic bore to its total operating expenses for the year within the state (a method protested by the State).

This was a debit item as to the G. N., but a very substantial credit item for the N. P., which possibly explains the difference in the attitude of counsel for the two companies.

Before specifically pointing out the different results reached by the State's and railroads' witnesses, it is thought appropriate at this point to discuss the various Assignments of Error involving the admissibility of evidence and the propriety of the appellant railroad's methods of apportioning operating expenses, taxes, and joint facility rents.

ASSIGNMENT NP-3*

COURT'S ERROR IN PERMITTING N. P.'s WITNESS, PETERSON, TO TESTIFY AS TO RELATIVE AMOUNT OF FREIGHT TRAFFIC DURING TEST WEEK AND ENTIRE YEAR 1933.

The N. P.'s claim that it lost money on its intrastate business for 1933 was based as above noted, on a purported special study of line-haul intrastate freight traffic during the week of October 22, 1933 (NP Rec. 89, *et seq.*), and a special study as to switching operations during the week of June 3, 1934. (NP Rec. 102, *et seq.*) For the purpose of attempting to show that this October test week was representative of the year's business, Peterson testified that a study was made for the purpose of comparing the relative revenues earned and ton miles and car miles operated during October and said test week in October, with the total for the year. (NP Rec. 89.) The State's counsel objected to any testimony as to such study if the same was based on entries in the company's books not introduced in evidence. (NP Rec. 90.) The objection being overruled, the witness testified to such comparative figures, from which he concluded that October was more favorable to both intra and interstate traffic than the average for the year. He further testified that to obtain the figures for October, 1933, he had the auditor of freight receipts make a special compilation, which figures were not reported to the D. P. W. (NP Rec. 90.) The court thereupon denied

*(NP 3) The court erred in permitting the N. P.'s witness, Peterson, to testify over objection that the same was hearsay and that the underlying data was not produced, as to the relative ton miles, revenue and average miles of haul of Washington traffic in October, 1933, and during the week of October 22, 1933, as compared with the entire year, and in refusing to strike such testimony after received. (NP Rec. 90-92.)

the State's motion that the testimony with respect to such comparative figures be stricken as hearsay and as based on the company's books not introduced in evidence. (NP Rec. 91.) The witness then testified over objection of the State's counsel as to the same kind of a comparison made with respect to the week of October 22, 1933, and the entire month of October. (NP Rec. 91-2.)

It would seem that the mere recital of these proceedings is sufficiently convincing that this evidence was not admissible under the hearsay and best evidence rules. Not only were the books not produced, but the individual who, it is claimed, took this data from the original records was not produced as a witness. Neither was this data (for the month and test week) reported to any state department. It would seem that in a proceeding in which a state law is assailed as unconstitutional, the State's counsel should not be left in a position where it is entirely impossible for him to verify figures and conclusions sought to be injected into the record in violation of some of the most fundamental rules of evidence.

The evidence, we submit, was not admissible.

ASSIGNMENT NP-4*

COURT'S ERROR IN RECEIVING IN EVIDENCE N. P.'s EXHIBIT "7" OVER OBJECTION THAT SAME WAS BASED ON HEARSAY AND RECORDS NOT RECEIVED IN EVIDENCE.

N. P. Exhibit "7" consisted of 22 pages of set-ups and computations based upon the special traffic study made during the week of October 22, 1933. (NP Rec. 93-4.)

This exhibit was received in evidence over the State's objection that the same was hearsay, largely based on conclusions and on estimates not made by a qualified expert, and from data taken from books not introduced in evidence and which the State's counsel had no opportunity to examine, and compiled by persons whom the State's counsel was given no opportunity to examine. (NP Rec. 101-2.)

As pointed out under Assignment NP-3, the value of the exhibit hinges on whether or not the test week chosen was representative of the year's traffic. The data bearing upon whether or not this was in fact a representative week was based upon records not received in evidence and the individual who took such data from the company's books was not even called as a witness.

Moreover, it appears that the revenues shown upon the N. P.'s books and reported under oath to the D. P. W. as the revenues received from intrastate freight traffic were not used in the preparation of such exhibit, but a lesser figure resulting from deducting therefrom certain revenues claimed to have been derived from

*(NP 4) The court erred in receiving in evidence N. P.'s Exhibit "7" over objection that the same was hearsay, and that the data upon which based was taken from the N. P.'s records not introduced in evidence. (NP 101-2.)

interstate or foreign shipments and switching although theretofore reported under oath to the D. P. W. as intrastate revenues. Mr. Peterson testified that these deductions were taken from the answers to interrogatories submitted by the N. P. (NP Rec. 94.) This is not the fact. No deductions of any kind were made in the answers to interrogatories *sworn to be true* by the N. P.'s assistant general auditor. (NP Rec. 78-9.) They were taken instead from so-called supplemental answers to interrogatories, verified by Mr. da Ponte, one of the N. P.'s attorneys, who only avers such answers to be true "to the best of affiant's knowledge and belief." (NP Rec. 84.) Da Ponte most certainly would not have been qualified to testify as an accountant. How, then, can his affidavit on mere information and belief be deemed to override the positive sworn statement of the N. P.'s assistant general auditor, and the sworn report to the D. P. W. which the N. P. itself introduced in evidence? (NP Ex. "9," Rec. 284.)

This information was contained in the records at the N. P.'s storage elevators (NP Rec. 151) and there is nothing to show that the same could not have been readily produced.

As shown under Assignment NP-17 (Post, pp. 131-133), the deductions attempted to be made as so-called interstate switching revenue were not shown by any exhibit of any kind although the records from which such showing might have been made were available in the state. (NP Rec. 248.)

Without going into further detail, we submit that, for the reasons shown, N. P.'s Exhibit "7" was not admissible and should be disregarded.

ASSIGNMENT NP-5*

COURT'S ERROR IN FINDING THAT N. P.'s METHOD OF APPORTIONING OPERATING EXPENSES TO ITS WASHINGTON TRAFFIC IS CORRECT.

In support of this assignment we need hardly do more than call attention to the following footnote that appeared in the N. P.'s report to the D. P. W. and tax commission for 1933 and for a number of years theretofore (NP Rec. 117):

"The statements herein either of revenues or expenses attributed to Washington are misleading unless properly understood. They are necessarily based on arbitrary assumptions as follows:

"Revenues contain (first) the revenues of business wholly local within the State and in addition a proportion of interstate revenues determined by the proportion of mileage which each interstate freight shipment or passenger is carried within the State.

"Charges for expenses contain (first) those expenses incurred in each state, and are considered wholly applicable to that state, and in addition some mileage proportion of expenses which cannot be localized. *Apportioning either such revenues or such expenses on a mileage basis is purely arbitrary* and has been adopted for want of any other basis." (Italics ours.)

Asked whether in his opinion the method used for apportioning operating expenses to Washington was the best method that can be used for the purpose of determining the propriety of rates both in this and other states, N. P.'s witness, Mr. Peterson, replied:

"I think each question there will have to depend largely on the local situation. You ask whether or not, for the purpose of determining the propriety of a local

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*(NP 5) The court erred in finding that the method used by the N. P. in assigning operating expenses to its Washington properties is the method prescribed by the D. P. W., and that the expenses incurred in Washington by the N. P. were correctly stated in Finding VI. (Finding VIII-b, NP Rec. 36-7.)

rate in any one of the states traversed by the N. P. the method used in the apportionment of these operating expenses as I have reported them to the state of Washington is the best method that could be used for the purpose of making such apportionment. I would say no. You ask me why. Well, because the conditions are constantly changing." (NP Rec. 118.)

We can only wonder if Mr. Peterson's replies were not actuated by apprehension that perhaps his answers might be used against him later in some rate hearing in the middle or "bridge" states.

Operating expenses incident to maintenance of way and structures, with the exception of superintendence, insurance, stationery and printing and "general" were practically all, Mr. Peterson testified (NP Rec. 115), directly assignable to Washington.

Mr. Peterson testified further:

"The expenses incident to all terminal services rendered within the state as to both interstate and intrastate traffic are all apportioned directly to the state. In addition to the actual operating expenses that are incident to the terminal services, the N. P. maintains large terminal facilities, such as docks, warehouses, yards, repair shops, depots, and so on in the larger cities of the state of Washington," etc. (NP Rec. 123.)

And see also the testimony of Mr. Lonergan. (NP Rec. 172-3.)

This, we submit, is an important reason why the N. P.'s method of apportioning operating expenses to Washington is indefensible in a case in which its true earnings from local business is in issue. Washington is a terminal state where the long-haul interstate business is assembled and distributed. The intermediate or "bridge" states have no terminal facilities comparable with the terminal states. (NP Rec. 128.) C. R. Loner-

gan, since 1927 chief of traffic division of the D. P. W., and for 33 years in the N. P.'s employ in various capacities, including that of traveling freight agent, general agent, assistant general freight agent, general freight agent, and assistant to the vice-president in charge of traffic (NP Rec. 172), testified:

"I am familiar with the method of accounting of the N. P. to the state of Washington in accounting for its railway operating expenses. (NP Rec. 173.) * * *

"The objection to the apportionment of all of the expenses connected with the maintenance of way and structures of a terminal state such as Washington as applies to the N. P., to the state of Washington, and the apportionment of none of those expenses whatever to the bridge state is that it does not place the proper charge upon interstate traffic; it places it all where it is expended, in the state of Washington. The terminal facilities located in Washington are of benefit to the traffic traversing the intermediate states, and in my opinion some of that expense should be apportioned to those intermediate states. That should also be true in regard to the maintenance of the terminals in Wisconsin and Minnesota. That should likewise be apportioned to this state and to the intermediate states as well. A portion of the taxes imposed by the state of Washington on the N. P. terminal facilities in Washington should likewise be apportioned to the bridge states, for the *same reasons* I have stated." (NP Rec. 175-6.)

It follows, of course, that if it is improper that all the terminal expense be assigned to Washington, an unjust maintenance expense burden must fall on intrastate business when such total terminal expenses are divided between Washington intra and interstate business according to relative freight car miles as was used in the N. P.'s special study. (See NP Ex. "7," p. 19, NP Rec. 167.)

We submit that a method of apportionment of expenses between states which the N. P., in its reports,

concedes to be "purely arbitrary" (NP Rec. 117-8), cannot yield results from which the court can set aside a state tax on the theory that this appellant is losing money in the state.

ASSIGNMENTS NP-6 TO NP-8*

COURT'S ERROR IN FINDING THAT STATE CONTENDED THAT N. P. SHOULD CREDIT PART OF ITS MAIL AND EXPRESS REVENUE TO LOCAL BUSINESS (NP AB. 288) AND IN FINDING THAT ANY PART OF SUCH REVENUE SHOULD BE APPORTIONED TO INTRASTATE.

These findings are wholly unsupported by the record. The State's only contention with respect to the N. P.'s revenues from mail and express was in connection with the method adopted by N. P.'s witness Peterson in apportioning passenger operating expenses between intra and interstate traffic. Peterson had prepared an exhibit in which he apportioned such expenses on a relative passenger mileage basis. (NP Ex. "7," p. 11.†)

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*(NP 6) The court erred in finding that plaintiff contended that the N. P. should credit part of its mail and express revenue to local business, whereas no such contention was in fact made. (Finding XII, NP Rec. 43-4.)

(NP 7) The court erred in finding that $221,359 or any other sum should be added to the N. P.'s intrastate passenger revenue for 1933, for intrastate mail and express, such finding being wholly unsupported by the record. (Findings IX-h, IX-i and IX-j, NP Rec. 40-41.)

(NP 8) The court erred in finding that the N. P.'s intrastate passenger revenue for 1933 was any sum greater than $429,635 as shown by plaintiff's Exhibit "25." (Finding IX-j, NP Rec. 42, 212A.)

†Defendant's Exhibit "7," p. 11, was omitted from the printed Transcript of Record, possibly because of its being inadvertently omitted from the transcript certified to this court by the clerk of the State supreme court. The same has now been properly certified to

The State sought to show on cross-examination (NP Rec. 132-3) that the use of this method wholly ignored the expenses incurred in connection with mail and express traffic, all of the revenues from which were assigned by the N. P. to interstate traffic. (NP Rec. 132.) *There is not a suggestion in the record that counsel for the State ever made the slightest objection to the apportionment of all mail and express revenue to interstate.* Counsel for the N. P. thereafter had Peterson prepare another exhibit apportioning a certain proportion of this mail and express revenue to intrastate based on relative passenger miles (NP Ex. "53," p. 2; NP Rec. 229), but without the slightest basis therefor since Peterson conceded what the court well knows to be the fact, that there is no relation between the proportion of interstate passengers and the proportion of interstate mail and express carried on a given train. Peterson testified:

"You ask if, as a matter of fact, it is impossible to make any apportionment of mail and express. It is, unless you consider that the mail that moves on local

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this court, but not having been printed as part of the Transcript of Record, it is herein set forth, as follows:

Def.'s Ex. "7," p. 11

NORTHERN PACIFIC RAILWAY COMPANY

State of Washington—Year 1933

Passenger proportion of Operating Expenses, Intrastate.		
Total passenger proportion of Operating Expenses year 1933, Intra and Interstate		**$3,142,708**
Revenue Passenger miles		**%**
Intrastate	**18,052,604**	**47.76**
Interstate	**19,749,788**	**52.24**
	37,802,392	**100.00**
Passenger proportion of Operating Expenses as applicable to Intrastate Traffic 47.76% of $3,142,708 or		**1,500,957**

trains is intrastate mail. That is the only way. That is not used. You ask if you can safely assume that. *No, I can't assume it, it is a false assumption.*" (NP Rec. 141.)

And again:

"You ask how much money the lines in the state of Washington realize from local mail and local express. I don't know. We know there is some, but the matter of division is a matter I can't inform you on." (NP Rec. 209.)

And again asked as to the relation between such revenue and passenger miles, he said:

"You ask if it is not true that I don't know anything about the relation. I can't give an exact opinion of the relationship, no." (NP Rec. 210.)

Counsel for the N. P. was, of course, actuated by no mere spirit of generosity in attempting to slough off a part of this mail and express revenue to intrastate traffic. He realized that whereas the total passenger revenue, intrastate and interstate, for 1933 was only $1,351,082 (Plff.'s Ex. "25," NP Rec. 212a), the operating expenses in connection therewith were $3,142,708 (Plff.'s Ex. "26," NP Rec. 217); *i. e.*, that the reported expenses were 232% of the reported revenues. Consequently the more passenger business he could donate to local operations, the more operating expenses he could pile up on the intrastate side of the ledger.

The offending findings should, we submit, be wholly ignored.

ASSIGNMENTS NP-9 AND NP-10*

COURT'S ERROR IN FINDING THAT N. P.'s PASSENGER SERVICE OPERATING EXPENSES SHOULD BE APPORTIONED TO INTRASTATE ON RELATIVE PASSENGER MILE BASIS INSTEAD OF RELATIVE REVENUE BASIS.

As part of its purported operating expenses, the N. P. made the following charge:

> "Passenger proportion of operating expenses applicable to Intrastate Traffic..... $1,500,957."
> (N. P. Ex. "7," p. 11; NP see footnote *ante*, pp. 105-6.)

This result was reached by apportioning the total intra and interstate operating expenses incident to Washington passenger traffic ($3,142,708) to intrastate traffic on the basis of relative passenger miles hauled in intra and interstate service. In so doing, the N. P.'s witness wholly ignored the obvious fact that its passenger trains are operated largely for the purpose of hauling express and mail, all of the revenues from which are apportioned to its interstate business. (Plff.'s Ex. "25," accts. 106-7, NP Rec. 212a:) It is, of course, clear that the relative number of Washington interstate and intrastate passengers hauled one mile has no logical relation to the amount of mail and express hauled on the passenger trains accommodating passengers. This was virtually conceded by N. P.'s witness Peterson, who prepared the exhibit. (NP Rec. 132-3.)

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*(NP 9) The court erred in finding that the correct method of apportioning the N. P.'s passenger service operating expenses as between intra and interstate passenger service is in the relation of relative revenue passenger miles, and not relative gross revenues. (Finding IX-i, NP Rec. 41-2.)

(NP 10) The court erred in finding that the N. P.'s expense of intrastate passenger business for 1933 was $1,500,000, or any other sum greater than $999,381 as shown by plaintiff's Exhibit "26." (Finding IX-j, NP Rec. 42.)

Take, for example, the passenger trains operating between Seattle and Grays Harbor. These trains, as we well know, are operated principally to afford mail and express service, yet, according to the N. P.'s theory, if on an average ten revenue passengers were carried or these trains, only one of which was an interstate passenger, then 90% of the operating expenses would be apportioned to the N. P.'s intrastate passenger service, although all of the revenue from mail and express is apportioned to interstate operations. Such an apportionment of expense, is, of course, wholly indefensible. Expenses must logically be apportioned as between intra and interstate operations with reference to the relative amount of interstate and intrastate business handled, and *since relative revenues is our only available data* as to the relative amount of intra and interstate passenger train business done (including mail, express, milk and other activities; see Plff.'s Ex. "25"; NP Rec. 212a) it is, we submit, impossible to conceive of how these expenses can logically be apportioned on any basis other than relative revenues. And were further justification for our position necessary, we need but turn to the G. N. exhibits, where we find the G. N. apportioning passenger operating expenses by precisely the method we urge here. To quote (G. N. Ex. "11," p. 7; GN Rec. 265-6):

"2. PASSENGER PROPORTION OF OPERATING EXPENSES—INTRASTATE:

"(a) Passenger proportion of operating revenues Intrastate and Interstate	$1,540,264
"(b) Passenger proportion of operating expenses—Interstate and Intrastate—as reported to W. D. P. W.	2,481,136
"(c) Operating Ratio	161.09%*
"(d) Intrastate Operating Revenues Passenger proportion	551,845

"(e) Intrastate Operating Expenses—Passenger proportion (d) × (c) ..... 888,967"

*Arrived at by dividing (b) by (a)—expenses by revenues.

Thus, in making its apportionment, the G. N. first finds the ratio of passenger operating expenses, both interstate and intrastate, to passenger operating revenues, both interstate and intrastate, and applies that ratio (161.09%) to the total intrastate passenger operating revenues to ascertain the passenger service proportion of intrastate operating expenses. In other words, it apportions its operating expenses as between intra and interstate passenger service on the basis of relative operating revenues from the two classes of service. That there may be no mistake, let us follow the G. N.'s method in the N. P. case:

"PASSENGER PROPORTION OF OPERATING EXPENSES—INTRASTATE:

"(a) Passenger proportion of operating revenues intrastate and interstate (Plff's Ex. "25"; NP Rec. 212a)	$1,351,082
"(b) Passenger proportion of operating expenses—Interstate and Intrastate (N. P. Ex. "7," p. 11; see footnote, *ante*, pp. 105-6)	3,142,708
"(c) Operating ratio (b ÷ a)	232.61%
"(d) Intrastate operating revenues, Passenger proportion (N. P. Ex. "7," p. 7, 1st figure in 5th line; Plff's Ex. "25," total of 2nd vertical column; NP Rec. 212a.)	429,635
"(e) Intrastate Operating Expenses—Passenger proportion ("d" × "c")	999,374"

And this figure, it will be observed, is just $7 less than the figure reached by plaintiff's witness, Manschreck, who followed the method here urged by plaintiff. (See Plff.'s Ex. "26," NP Rec. 213.)

But as shown, the N. P. charged $1,500,957 as its 1933 intrastate passenger operating expenses, or $501,-

576 more than can be reached on any reasonable theory. (N. P. Ex. "7," p. 11, see footnote, *ante* pp. 105-6.)

ASSIGNMENTS NP-11 AND GN-10*

COURT'S ERROR IN FINDING THAT THE MILEAGE PRORATE DIVISION OF REVENUES FROM INTERSTATE SHIPMENTS AS BETWEEN STATES IS THE CORRECT METHOD OF APPORTIONING SUCH REVENUES TO WASHINGTON.

Both the N. P. (N. P. Ex. "7," p. 7; NP Rec. 161) and the G. N. (G. N. Ex. "11," pp. "9," and "C;" GN Rec. 256, 267-8) contend that the ad valorem taxes on their respective operating properties in Washington should be apportioned between intrastate and interstate traffic in that proportion which the revenues from intrastate traffic bear to the revenues from interstate traffic. It is further conceded that for the purpose of determining the amount of such interstate revenue the total revenue from each interstate shipment is apportioned to Washington in that proportion which the miles of haul in Washington bear to the total mileage of haul as to each individual shipment. (NP Rec. 118-9; GN Rec. 127). The State contends in each case that this method of apportionment of taxes is improper, for the reason, if for none other, that this mileage prorate division, while it may do for purely statistical purposes, is

*(NP 11) The court erred in finding that the mileage prorate division of revenues from interstate shipments is the method prescribed by the D. P. W. and the I. C. C., and is the correct method for apportioning such revenues to Washington. (Finding VIII-a, NP Rec. 36.)

(GN 10) The court erred in finding that in the apportionment of operating revenues received from interstate freight business to the G. N.'s Washington operating properties, such properties were not entitled to more than a mileage prorate of such interstate freight revenues. (Finding VII-e, GN Rec. 65-7.)

purely arbitrary and is unfair to a terminal state such as Washington, and for this reason: The rate exacted for handling traffic involves at least two services, (1) the line-haul service, and (2) the terminal service. The terminal service is just as essential as the line-haul service, and falls most heavily on terminal states such as Washington where a large part of the profitable long-haul business originates and terminates. The mileage prorate is computed on a station-to-station movement only (GN Rec. 146; NP Rec. 120), and consequently, such apportionment method wholly ignores both the terminal service rendered and terminal expenses incurred in the movement. Thus, Mr. Peterson testifying for the N. P., said:

"The company furnishes a large amount of service in connection with the movement of that traffic (interstate) which is included in the tariff aside from the purely line haul. * * * I will say that it includes the large expenses in connection with switching, also handling of freight at terminals for both classes of traffic, both intrastate and interstate. * * * The assembling of the cars into the originating trains would involve some switching, none of which would be reflected in the mileage prorate division. The mileage prorate would include the line haul only." (NP Rec. 120-121.)

Mr. Burn of the G. N. testified substantially to the same effect. (GN Rec. 146-7.)

It is rather startling to compare the court's findings that the mileage prorate is "the method prescribed by the Department of Public Works" (NP Rec. 35), with the following testimony of Mr. Lonergan, since 1927 chief of the D. P. W.'s traffic division (NP Rec. 172):

"You ask me to state whether or not in my opinion such method of apportioning revenues followed by the N. P. is a proper method of apportioning revenues to

the state of Washington for the purpose of determining the true net railway revenues in the state. I would say not for ratemaking purposes. (NP Rec. 174.) * * *

"You ask whether it is my opinion that the interstate revenues should be apportioned to Washington on a mileage prorate. No. You ask why not. Because that division does not allow for the terminal service. In other words, if the expenses are to be apportioned locally, to the terminal state, then a greater proportion of the earnings or the revenues should be apportioned to that state. You should either apportion a certain proportion of the expenses connected with this terminal service to the remainder of the states, or you should apportion a greater percentage of the interstate revenues to the state to equalize those expenses. (NP Rec. 176.) * * *

"The rate is made to compensate for the haulage over the mountains. It is also made to cover cost of terminal services. The terminal service charge is absorbed in the line haul rate. The terminal services and the line haul service is all included as part of the structure of the service, the total service, to be paid for by the imposition of this tariff. If the computation of mileage is from station to station, the terminal service is in no way whatever reflected by the apportionment on a mileage prorate. It wholly ignores it and considers only the mileage of haul." (NP Rec. 182.)

"It is," Mr. Lonergan said, "a matter of common knowledge that these figures that are filed in the annual reports of the railroads covering their state revenues and expenses are incorrect." (NP Rec. 175.) With respect to the recognition of this principle by the D. P. W., Mr. Lonergan said:

"In all consideration of intrastate rates we have always taken into account these arbitrary assumptions that are contained in the state figures, and to quite an extent have disregarded them. That is, the mileage prorate which gives the state of North Dakota or Montana the same revenue per mile as it does in the state of Washington without regard to the terminal services, the absorption of competitive switching on interstate busi-

ness, and many other factors which distort the figures." (NP Rec. 175.)

And we find the D. P. W. making the following finding of fact in 1930 in a proceeding in which the G. N. and N. P. were parties:

"All of the operating cost figures are based upon the arbitrary allocation of revenues and expenses now employed under which interstate revenues are apportioned to states on basis of a mileage pro-rate. This disregards the terminal proportion of the revenue and gives the intermediate states as great a share in proportion to mileage as the states in which the traffic originates and terminates. It gives no consideration to relative costs in different states as constituting any measure of relative revenue which should be apportioned to such states. Non-revenue freight or company material is a large factor in the operating costs in Washington, but under the existing plan of localizing expenses to the state in which they occur, the costs of handling company freight is not distributed in proportion to their responsibility for the expenses. Absorption of competitive switching charges on interstate traffic and many other factors also contribute to distort the facts." (Plf.'s Ex. "24," NP Rec. 211-2.)

In this connection it is also important to note that in the division of revenues as between connecting carriers on through shipments, the originating and terminating carrier is commonly allowed far more than a mileage prorate division. The terminal line usually receives a minimum of 25% of the through rate with the local rate as the maximum.

Asked whether there was any general principle governing the apportionment of interline revenue as between two terminal lines and an intermediate line, Mr. Edmunds, assistant traffic manager of the Union Pacific System (NP Rec. 199; GN Rec. 247) testified:

"The basis most generally used has been a mileage prorate with a minimum of 25% to any line, whether the terminal lines or the intermediate line. The local rate is the maximum generally, yes. It might be less than 25%, depending on the agreement of the parties. These divisions would apply both west and east, to traffic going in both directions. As a rule the short line would get the 25% minimum whether it received the traffic or originated the traffic." (NP Rec. 201; GN Rec. 248.)

The Oregon-Washington ("O-W") operates between Portland and Huntington (on the Idaho-Oregon boundary); the Oregon Short Line ("O. S. L."), between Huntington and Granger, Wyoming; and the Union Pacific ("U. P.") between Granger and Omaha. Huntington corresponds roughly with the location of Spokane on the G. N. and N. P., and Omaha is approximately the same distance from Chicago as St. Paul. 100% of the O-W stock is owned by the O. S. L. and approximately all of the O. S. L. stock is owned by the U. P. On a shipment between Portland and Omaha the O. W. receives 35%, the O. S. L. 27% and the U. P. 38% of the through rate. On the same haul, the mileage prorate would give the O-W 22.05%, the O. S. L. 30.44% and the U. P. 47.51%. (NP Rec. 199-203; GN Rec. 247-50.)

A graph is set forth in the record (NP Rec. 228a; GN Rec. 250a) comparing the divisions as compared with the mileage prorate division between the O-W and the Milwaukee and G. N. east and west of Spokane, and as between the N. P. and O-W east and west of Wallula.

On shipments between the points on the Southern Pacific ("S. P.") and Omaha via the U. P. system, the S. P. receives about twice its maximum mileage prorate of the West of Missouri River revenue. (GN Rec. 252.)

The through rate on lumber from Longview points

to Omaha is 62.5 cents. Of this, the railroad there (before being absorbed by other roads) received 3½ cents for a 5-mile or 23-mile haul. (GN Rec. 253.)

A striking illustration of the inadequacy of the mileage prorate as to terminal states exists in the cases of Oregon and Wisconsin, as to which Mr. Peterson testified:

"The N. P. reports to the regulatory bodies of Oregon and Wisconsin: The states of Wisconsin and Oregon have a considerably higher expense because of the short mileage in the state and the terminal operations in that state. In making its reports to Wisconsin and Oregon regulatory bodies it uses the same basis of allocation to the state as it did the state of Washington. The net revenue from operation in the state shows a deficit for the year 1933 for Wisconsin and Oregon. I know that has been true for a good many years. No, I would not say that the lines in Oregon and Wisconsin are not a valuable part of the N. P. system. You ask if that means that the N. P. is not actually making money from its railway operations in Wisconsin and Oregon. We are making money probably from the operations as a whole, but not necessarily from the operations in that state. It does not mean that the N. P. system would profit by having the portion of its system located in Oregon and Wisconsin eliminated." (NP Rec. 121-2.)

It is interesting to note the trial court finds that the mileage prorate method is "the method prescribed by the * * * Interstate Commerce Commission." (NP Rec. 36.) Let us quote from a few of the I. C. C. decisions:

"Fundamentally, this statement proceeds on what we consider to be an erroneous theory; that is, that certain portions of a system of railroad can be segregated from the whole and the expenses and earnings be charged and credited to such portions on a mileage-prorata basis." *Investigation of Advances in Rates on Grain,* 21 I. C. C. 22, 25-26.

"It is to be expected that an originating division would apparently not be self-supporting any more than would the average large terminal in a city. To make them self-supporting it is necessary to assign to the originating division and to the terminal a sufficient portion of the revenues to more than offset the expenses. This would have to be an arbitrary sum. It could hardly be accomplished by the ordinary method of prorating the revenue or dividing it under a block-mileage system." *Louisville & Nashville R. R. Coal and Coke Rates,* 26 I. C. C. 20, 29.

"The apportionments of revenues, expenses, and other income items between the line of the United States and Canada and the lines of the Grand Trunk in Canada are in many instances made upon bases of road mileage, car-mileage, or train mileage. We have held that a portion of a railroad system can not be separated from the whole, and the earnings and expenses charged, and credited to such portion on a mileage prorate basis. *Investigation of Advances in Rates on Grain,* 21 I. C. C. 22, 25; *Louisville & Nashville R. R. Coal and Coke Rates,* 26 I. C. C. 20, 30. It is well known that a mileage prorate of transportation revenues or expenses will in many cases result in a showing of deficits for branch lines of light traffic density, notwithstanding the showing for the system as a whole is a substantial profit." *Deficit Status of U. S. & Canada R. R.,* 76 I. C. C. 455, 457-8.

It is to be particularly noted that these companies themselves each year set out in an impressive foot note in their reports to the D. P. W.:

"Apportioning either such revenues or such expenses on a mileage basis is purely arbitrary and has been adopted for want of any other basis." (NP Ab. 82.)

"The figures entered as 'revenues earned within the State on interstate traffic,' are compiled upon a straight mileage basis in accordance with order of the Railroad Commission and are given under protest for the reason that *this Company claims that basis does not accurately reflect the revenues earned within the state of Wash-*

ington from such traffic.'' (GN Rec. 147-8.) (Italics ours.)

We respectfully submit that by apportioning *ad valorem* taxes on the basis of the relation of intrastate earnings which are known, and interstate "earnings" apportioned to Washington, a terminal state, on this mileage prorate basis, the court would by these companies' own admissions, be resorting to most arbitrary and erroneous assumptions for the purpose of defeating the occupational tax. This, we are confident, the court will not do.

ASSIGNMENTS NP-12 TO NP-14*

COURT'S ERROR IN IGNORING TAXES PAID BY N. P.'s TENANT LINES, AND HOLDING THAT TAXES SHOULD BE APPORTIONED BETWEEN INTRA AND INTERSTATE TRAFFIC ON RELATIVE REVENUE BASIS.

The N. P.'s first error was in attempting to apportion the entire amount of *ad valorem* taxes payable on its Washington operating property ($2,005,015) to its intra and interstate operations (N. P. Ex. "7," p. 7; NP Rec. 161) whereas $227,600.74 of these taxes were in fact paid by its tenant companies. (Plff.'s Ex. "28;" NP Rec. 214.) Thus, in reality, the N. P. paid in taxes on its operating properties only $2,005,015 less $227,601, or $1,777,414.

Having determined the correct figures, how should these taxes be apportioned as between the N. P.'s Washington intrastate and interstate freight operations? On a relative revenue basis? We submit not. If A and B have the joint use of a private roadway and A uses the same four times as much as B, clearly A should equitably pay 4/5ths of the taxes payable by A and B jointly. And it is immaterial, we submit, whether B receives pro-

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*(NP 12) The court erred in finding that the 1933 ad valorem taxes on the N. P.'s Washington operating property should not be apportioned as between intrastate and interstate traffic on a relative use (car-mileage) basis, but instead on a relative revenue basis, with interstate freight revenues apportioned to Washington on a mileage prorate basis. (Finding XII, NP Rec. 43-4.)

(NP 13) The court erred in finding that in computing the ad valorem taxes properly apportionable to the N. P.'s intrastate traffic for 1933, credit should not be allowed such traffic for the taxes contributed by the N. P.'s tenant lines. (Finding XII, NP Ab. Rec. 43-4.)

(NP 14) The court erred in finding that the N. P.'s intrastate traffic for 1933 should be charged with ad valorem taxes paid in the sum of $876,083 or any greater sum than $678,662. (Finding XI-b, NP Ab. Rec. 43, 215-6.)

portionally more gross revenue from his use of such roadway than does A. To support our contention, we need fortunately go no further than the N. P.'s own agreements with the G. N. and O. W. for the joint use of the N. P.'s tracks between Portland and Seattle. The N. P. owns these tracks but the G. N. and O-W. use them in their railway operations jointly with the N. P. For this privilege the G. N. and O-W. pay the N. P. an annual rental based on a certain percentage of the cost of construction plus betterments, and in addition, contribute a certain proportion of the taxes paid on this portion of the N. P.'s road. Now how are those taxes apportioned as between the N. P., G. N. and O-W.? According to the relative amount of gross revenue received by each carrier? No. *The taxes are apportioned according to the relative amount of use made of such property by the respective roads.* To quote from the O-W. agreement (p. 13, Sec. 2):

"The Oregon Company (O-W.) also will pay such pro rata proportion of the cost actually incurred by the Pacific Company (N. P.) in the maintenance and operation of the Point Defiance Line (which cost shall include insurance and *taxes* and a just sum to cover cost of superintendence and management) as the number of miles on the said railway or any part thereof run by engines and cars in its trains bears to the whole number of miles run by engines and cars in trains of all the parties using the same or any part thereof." (NP Rec. 156.)

And further quoting from the G. N. agreement (p. 6, sec. 2):

"The Northern Company (G. N.) will also pay such pro rata proportion of the cost actually incurred by the Pacific Company (N. P.) in the maintenance and operation of the property (which cost shall include insurance and taxes and a just sum to cover cost of superinten-

dence and management) as the number of miles on said railway or any part thereof run by engines and cars in its trains bears to the whole number of miles run by engines and cars in trains of all the parties using the same or any part thereof." (NP Rec. 131.)

This, then, is the way these litigants by their own voluntary agreements apportion taxes as between themselves. Nor have they offered any valid reason for apportioning taxes on a different basis as between intrastate and interstate operations. It is to be noted that no distinction is made in these joint user agreements as between passenger and freight train cars.

Nor are we without authority. In the *Minnesota Rate Cases*, 230 U. S. 352, certain railroad companies including the N. P. and G. N. were contending that certain intrastate rates fixed by the Minnesota regulatory authority were confiscatory, as not yielding a fair return upon that portion of the complaining carriers' operating property used in intrastate operations. Having established the value of all of their respective Minnesota operating properties used in both interstate and intrastate operations, they then attempted to apportion such value as between their interstate and intrastate operations on the basis of relative gross revenues received in these two classes of service. But in condemning this method the court said (230 U. S. p. 458 *et seq.*):

"The apportionment of the value of the property, as found, between the interstate and intrastate business, was made upon the basis of the gross revenue derived from each. This is a simple method, easily applied, and for that reason has been repeatedly used. It has not, however, been approved by this court, and its correctness is now challenged. * * *

"In support of this method, it is said that a division of the value of the property according to gross

earnings is a division according to the 'value of the use,' and therefore proper. But it would seem to be clear that the value of the use is not shown by *gross* earnings. The gross earnings may be consumed by expenses, leaving little or no profit. * * *

"When rates are in controversy, it would seem to be necessary to find a basis for a division of the total value of the property independently of revenue, and this must be found in the use that is made of the property. That is, there should be assigned to each business that proportion of the total value of the property which will correspond to the extent of its employment in that business. It is said that this is extremely difficult; in particular, because of the necessity for making a division between the passenger and freight business, and the obvious lack of correspondence between ton-miles and passenger-miles. It does not appear, however, that these are the only units available for such a division; and it would seem that, after assigning to the passenger and freight departments respectively, the property exclusively used in each, comparable use-units might be found which would afford the basis for a reasonable division with respect to property used in common. It is suggested that other methods of calculation would be equally unfavorable to the state rates but this we cannot assume.

"It is sufficient to say that the method here adopted is not of a character to justify the court in basing upon it a finding that the rates are confiscatory."

In brief, the Supreme Court holds that the value of operating property should be apportioned as between such interstate and intrastate business in proportion to the *extent* of the use made of such property in each business, and not in proportion to the relative gross revenue derived therefrom.

And since taxes are based upon property *values* it must logically follow that the relative amount of taxes chargeable to each of two kinds of business jointly utilizing the same property must be determined by the same

method; namely, by the *relative extent of use* made of the joint property in such two classes of business—not by the relative gross revenues derived therefrom.

The N. P., as already shown, has used the gross revenues method condemned by the Supreme Court. The State, on the contrary, has apportioned taxes on the basis of relative extent of use, the method approved by the Supreme Court.

Thus, in Plaintiff's Exhibit "29" (NP Rec. 215-6) Mr. Manschreck first finds the ratio of total state *passenger* car and locomotive mileage to total state *freight and passenger* car and locomotive mileage to be 15.91%. He therefore apportions 15.91% of the total N. P.'s taxes to passenger service and the remainder (84.09%) to freight service. The ratio of interstate freight car mileage to total of intra and interstate freight car mileage for the test period was found by defendant to be 42.30%. (N. P. Ex. "7," p. 13; NP Rec. 164.) Manschreck therefore apportions 42.30% of the total taxes apportionable to state intra and interstate freight service to intrastate freight service, or $632,227. There being no other factor available, Manschreck finds the ratio of intrastate passenger revenue to the total intra and interstate passenger revenue and apportions to intrastate passenger operations that percentage (31.80%) of the total taxes apportionable to both intra and interstate passenger service, or $89,926, making a total of $722,153. This added to the $13,236 regulatory license tax makes a grand total of $735,389 apportionable to Washington intrastate operations. The taxes apportioned to this service under the N. P.'s calculations, are $889,319, or $153,930 less than the maximum apportionable by the proper method used by Mr. Manschreck.

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But if the N. P. is to be allowed to transfer $369,606 reported under oath to the D. P. W. as intrastate freight revenue, to interstate freight revenue, then obviously Mr. Manschreck has apportioned too much taxes to intrastate freight traffic. Mr. Manschreck's figures were based on the assumption that all of the freight business reported as intrastate was in fact intrastate. The total freight revenues reported by the N. P. as intrastate were $5,372,895 (Plff.'s Ex. "25," NP Rec. 212a, 1st vertical column). The N. P. contends (erroneously as we will show later) that $369,606, of this revenue was in fact revenue derived from shipments for export and therefore foreign and not intrastate traffic. Since we are not furnished with data as to the corresponding number of freight car miles involved, we are compelled to assume that a reduction should be made corresponding with the revenue involved, *i. e.*, in the relation of $369,606 to $5,372,895, or 6.879%. This percentage of $632,227 (the taxes Manschreck found should be apportioned to intrastate freight service) is $43,491. Deducting this amount from the grand total of taxes which Manschreck found should be apportioned to intrastate freight and passenger traffic, we have $735,389 less $43,491, or $691,898, or $197,421 less than the $889,319 reached by the N. P.'s calculations.

It will be observed in making this modified calculation we have ignored the $161,031 which the N. P. contended should be transferred from its reported intrastate switching revenue, to interstate. (NP Ex. "7," p. 4; NP Rec. 159-160.)

ASSIGNMENTS NP-15 AND GN-13*

COURT'S ERROR IN FINDING THAT PENSIONS PAID WERE PROPERLY CHARGEABLE AS PART OF THE N. P.'s AND G. N.'s OPERATING EXPENSES.

It was shown that if "pensions" were eliminated as an item of operating expense, the operating expenses incident to intrastate traffic would be reduced by at least $103,471 in the case of the N. P. (Plff.'s Ex. "37," NP Rec. 231, Test. of Manschreck, NP Rec. 191-2), and $22,066 in the case of the G. N. (Plff.'s Ex. "25," GN Rec. 233-4.)

Mr. Manschreck's computation as to the G. N. was based on the G. N.'s "book showing," *i. e.*, the assumption that all its operating revenues reported as intrastate were in fact intrastate. If, however, the court finds it to be established by competent evidence that a certain amount of the G. N.'s revenues reported as intrastate, should be transferred to interstate, then its intrastate freight revenue for 1933 would be $1,622,644 (G. N. Ex. "11," p. "B," GN Rec. 255), instead of $2,753,703 as shown by its books and sworn report to the D. P. W. (GN Ex. "11," p. 11, GN Rec. 268a), and this item of $22,066 would have to be reduced to an amount represented by the proportion which $1,622,644 bears to

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*(NP 15) The court erred in finding that the N. P.'s total intrastate freight operating expenses classified as "General Expenses," for the week of October 22, 1933, was $5,945.44, or was any sum in excess of $4,407.89, which error was the result of the court including "pensions" as an item of operating expenses. (Finding IX-e, NP Rec. 39, 221.)

(GN 13) The court erred in finding that pensions paid were properly chargeable as part of the G. N.'s operating expenses for the purpose of determining its railway operating income for 1933. (Finding VII-j, GN Rec. 69.)

$2,753,703, or 58.92%, making the amount 58.92% of $22,066, or $13,001 only.

However commendable the practice of these roads of paying pensions, we cannot believe it a good defense in an action for a legitimate tax, that the company elects to pay pensions to its ex-employes and hence cannot pay the contested tax without drawing on its interstate earnings.

Mr. Manschreck testified in the G. N. case:

"My thought on the pensions was that pensions are a donation by the owners of this property to its former employees, and would be in the same class as paying dividends on this stock. I think pensions should be charged to profit and loss, and not to operating expenses. I think this is a gift or a grant. I don't think it is deferred compensation to those employees." (GN Rec. 224.)

In Railroad Retirement Board v. Alton R. Co., — U. S. —, 55 Sup. Ct. 758, 770-773, the court said in holding invalid the Federal Compulsory Retirement and Pension Act:

"We think it cannot be denied and indeed, is in effect admitted, that the sole reliance of the petitioners is upon the theory that contentment and assurance of security are the major purposes of the act. We cannot agree that these ends if dictated by statute, and not voluntarily extended by the employer, encourage loyalty and continuity of service. We feel bound to hold that a pension plan thus imposed is in no proper sense a regulation of the activity of interstate transportation. It is an attempt for social ends to impose by sheer fiat noncontractual incidents upon the relation of employer and employee, not as a rule or regulation of commerce and transportation between the states, but as a means of assuring a particular class of employees against old age dependency. This is neither a necessary nor an appropriate rule or regulation affecting the due fulfillment

of the railroads' duty to serve the public in interstate transportation."

If the payment of pensions to superannuated employees is not a duty which regulatory bodies may lawfully impose on public service companies, does it not logically follow that if such companies, voluntarily elect to pay such pensions, they are not at liberty to set up such payments as claims against their gross operating revenues superior to the right of the sovereign authority to collect its taxes? We submit not, Your Honors.

ASSIGNMENT NP-16*

COURT'S ERROR IN FINDING THAT $530,637, OR ANY OTHER SUM WHICH WAS REPORTED BY THE N. P. TO THE D. P. W. FOR 1933 AS INTRASTATE FREIGHT REVENUE WAS IN FACT INTERSTATE REVENUE.

The first item on page 4, NP's Ex. "7" (Ab. NP Rec. 159) is as follows:

"Operating revenues State of Washington Intrastate as reported to Department of Public Works.....$5,802,530."

There is then deducted from this amount the sum of $530,637 as "deduction account of amount as included in connection with foreign commerce $369,606," and "deduction account of switching in connection with interstate traffic included as intrastate, $161,031."

There is, we submit, nothing in the record justifying these deductions. These revenues, as indicated by the exhibit itself, were reported to the D. P. W. intra-

*(NP 16) The court erred in finding that $530,637, or any other sum reported by the N. P. to the D. P. W. for 1933 as intrastate freight revenue was in fact interstate revenue. (Finding X, NP Rec. 42-3.)

state revenues. That this was true was likewise testified to by Mr. Peterson, defendant's statistician. (Plff.'s Ex. "25," NP Rec. 182, 212a.)

Counsel for the N. P. seem to justify these deductions by certain purported supplemental answers to interrogatories filed in the cause by this appellant's counsel. But this, we submit, is no justification whatever. The N. P. filed with the D. P. W. its report for 1933, sworn to be the Assistant General Auditor to the following effect:

"That it is his duty to have supervision over the books of account of the respondent and to control the manner in which such books are kept; that he knows that such books have, during the period covered by the foregoing report, been kept in good faith in accordance with the accounting and other orders of the Interstate Commerce Commission, effective during the said period; that he has carefully examined the said report and to the best of his knowledge and belief the entries contained in the said report have, so far as they relate to matters of accounts, been accurately taken from the said books of account and are in exact accordance therewith; that he believes that all other statements of fact contained in the said report are true, and that the said report is a correct and complete statement of the business and affairs of the above-named respondent during the period of time from and including January 1, 1933, to and including December 31, 1933." (N. P. Ex. "9," NP Rec. 284.)

Such report was also sworn to by the company's vice president to the effect that he has carefully examined the foregoing report; that he believes that all statements of fact contained therein are true, and that the said report is a correct and complete statement of the business and affairs of the N. P. and the operations of its property during the year 1933. (NP Ex. "9," p. 915, NP Rec. 284.)

On page 700 of this report (NP Rec. 275) the revenues of the N. P. on intrastate traffic are shown to have been $5,802,530.12.

In the N. P.'s answers to interrogatories the revenues of the N. P. on intrastate traffic are set forth for each of the months of August, September, October, November, and December, 1933, both by accounts and in the total amounts, and such answers are verified by W. C. Pinger, defendant's assistant general auditor, who avers:

"That he prepared the foregoing answers to the interrogatories propounded by plaintiff and made the same for and in behalf of said Northern Pacific Railway Company; that said answers are to affiant's knowledge true and correct." (Plff.'s Ex. "2," NP Rec. 78-9.)

Then on June 27, 1934, a paper is filed denominated "Defendant's Second Supplemental Answers to Interrogatories" in which it is stated that certain amounts should be deducted from the amounts shown under account No. 101 in the original answers to interrogatories. But these so-called "supplemental answers" are merely verified by L. D. da Ponte, attorney for defendant, to the effect that the same are "true and correct to the best of affiant's knowledge and belief." (NP Rec. 84.) Moreover, not a word is said in these so-called supplemental answers as to switching in connection with interstate traffic.

We have then, on the one side, the N. P.'s report to the D. P. W. sworn to by the N. P.'s assistant general auditor and vice-president that the N. P.'s intrastate revenues for 1933 were $5,802,530, and the answers to interrogatories sworn to by the N. P.'s assistant general auditor that the same are *"to affiant's knowledge,*

true and correct," and on the other, the affidavit of one of the N. P.'s attorneys that to the best of his knowledge and belief, the original answers to interrogatories are erroneous in certain particulars. Whom should the court believe? The sworn report of the company's vice-president and assistant general auditor who are in a position to know, and the sworn statement of the company's assistant general auditor that the answers to interrogatories are correct, or the attempted controverting statement of counsel sworn to merely on information and belief with no averment that he has knowledge of the facts? Had counsel attempted to testify at the trial as to the matters set forth in his affidavit he of course could not have qualified as such witness. How, then, can it be said that his written statement sworn to merely on information and belief, can change the effect of the assistant general auditor's sworn statement? We submit that Mr. daPonte's statement should be utterly disregarded, and the company's report and the original answers to interrogatories should be accepted as undisputed evidence.

See 32 C. J. 354, 357;
Lake Shore & M. S. Ry. Co. v. Felton (C. C. A.), 103 F. 227;
Behre v. Anchor Ins. Co. (C. C. A.), 297 Fed. 986;
Pine-Coffin v. Erie R. Co., 69 N. Y. S. 333.

Unless Mr. daPonte's affidavit made on mere information and belief be held to overcome the positive sworn statement of the company's assistant general auditor, and the company's verified report to the state regulatory body, then N. P.'s Exhibit "7," p. 4 (NP Rec. 159-160), is erroneous and $530,637 must be added to the company's intrastate revenues for 1933.

But a corresponding amount of operating expenses must also be added. The relation of operating expenses to revenues is shown by N. P.'s Exhibit "7," p. 4, to be 68.06%. Consequently .6806 × $530,637 or $361,152 must be added to operating expenses, and the difference of $169,485 should be added to the "net revenue from railway operation" as shown in line "3," NP Ex. "7," p. 1, NP Rec. 159-160.)

ASSIGNMENT NP-17*

COURT'S ERROR IN REFUSING TO STRIKE AVERMENT IN PETERSON AFFIDAVIT THAT AMOUNT OF N. P.'s INTERSTATE SWITCHING REVENUE FOR 1933 WAS $207,965.

On November 13, 1934, the court, on the State's motion, reopened the case for the purpose of permitting it to introduce further evidence as to the matters set forth in Manschreck's affidavit (NP Rec. 232-241), and on November 16, 1934, the date set for such hearing, Manschreck's affidavit was received in lieu of his testimony, it being stipulated that the N. P. might file an affidavit in rebuttal thereto, but that the State might have the right to cross-examine such witness if it so desired. (NP Rec. 251.) Nothing was set forth in the Manschreck affidavit except a criticism of the calculations made, and conclusions reached, by Peterson in N. P. Exhibit "7," based on the special studies for the weeks of October 22, 1933, and June 3, 1934. (NP Rec. 232-241.)

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*(NP 17) The court erred in refusing to strike paragraph 7 of Peterson's affidavit to the effect that the amount of the N. P.'s interstate switching revenue for 1933 was $207,965 because not based on any record evidence before the court (NP Rec. 248-9.)

On November 26, 1934, the N. P. offered in evidence the affidavit of E. V. Peterson which was received in evidence over the State's said objection. (NP Rec. 242.)

In paragraph 7 of the Peterson affidavit above referred to it is stated that an analysis had been made for the year 1933 showing that the amount of the N. P.'s interstate switching revenue for 1933 was $207,965. (NP Rec. 245.) It will be recalled that this switching revenue was all reported to the D. P. W. as intrastate revenue (NP Rec. 132), but in the N. P.'s studies the N. P. attempted to transfer a large part ($161,031) from intrastate to interstate. (N. P. Ex. "7," p. 4; NP Rec. 159-160.)

With regard to this switching revenue, Peterson testified:

"You ask if it is not a fact that there is no record in the state of Washington anywhere, that would show these facts. No, the only report we furnished to the D. P. W. for 1933 was in Ex. '9,' the annual report, in which it showed the entire amount of switching revenue. It was all shown as intrastate. That was sworn to by our officers and filed. It was made March 4, 1934, and was made on the same basis of previous years. The record in the state would be available at the various stations. You ask if there is any record here to show the change in our book accounts. No, there is no record here. There is no record offered in exhibits of any kind that would tend to show whether these were interstate or intrastate movements. I couldn't do that without going to our records scattered around throughout different parts of the state or our records in St. Paul." (NP Rec. 248.)

The State's counsel thereupon moved to strike paragraph 7 as not based on anything shown of record, and because based on record evidence not produced, which motion was denied. (NP Rec. 248-9.)

For the reasons pointed out in the motion to strike we respectfully submit that this portion of the Peterson affidavit should have been stricken and the same disregarded.

ASSIGNMENT NP-18*

COURT'S ERROR IN FINDING THAT "TRAFFIC" EXPENSE SHOULD PROPERLY BE APPORTIONED BETWEEN INTRA AND INTERSTATE OPERATIONS ON A RELATIVE TONNAGE BASIS INSTEAD OF A RELATIVE REVENUE BASIS.

"Traffic" expenses are those incident to the solicitation of traffic. The purpose of such expenditures is to secure revenue-bearing traffic. It is logical, therefore, to assume that expenses in the solicitation of freight traffic are proportional to the amount of freight *revenue* received and not to the amount of *tonnage* originated. For example, the intrastate tonnage of logs for 1933 was 2,000,463 and all other intrastate freight, 1,776,398 (see N. P. Ex. "7," p. 16; NP Rec. 166.) We think the court judicially knows that the N. P.'s log traffic is largely if not entirely non-competitive. Consequently, little or no "traffic expense" can rightfully be charged to that kind of traffic. Yet said appellant apportions as much "traffic expense" to a ton of logs as to a ton of automobiles with perhaps ten times the revenue per ton mile.

Logs are a very low revenue-producing commodity. (NP Rec. 126.) The length of haul is very short even

*(NP 18) The court erred in finding that the N. P.'s total intrastate freight operating expenses classified as "Traffic Expenses" for the week of October 22, 1933, was $3,086.41, or was any sum in excess of $2,366.77, as shown by Exhibit "B" attached to the affidavit of State's witness, Manschreck. (Finding IX-e, NP Rec. 39, 241.)

as compared with other intrastate business. The greatest volume of this traffic is 18 miles. (NP Rec. 146.) Something, we submit, is decidedly wrong with a method of apportionment which assigns the same proportion of expense to a ton of logs hauled but a few miles, and to a ton of silk hauled 2,000 miles.

Mr. Manschreck apportioned these "traffic" expenses as between intra and interstate on a relative revenue basis, rather than on a relative tonnage basis (NP Rec. 241) which, we submit, yields a result as nearly correct as the limited data supplied by the N. P. permits. This apportions 50.149% to intrastate. The percentages apportioned by other possible factors would be as follows: relative freight car miles, 42.30%, relative gross ton miles, 41.92%; relative net ton miles, 46.47%. (NP Ex. "7," p. 13; NP Rec. 164.)

Using the relative revenue basis, the State's calculations in "Exhibit B" attached to the Manschreck affidavit (NP Rec. 241), shows that the N. P.'s 1933 intrastate freight expenses charged to "traffic" would have been $37,525.65 less, and its operating income correspondingly greater than as shown by N. P.'s Exhibit "7."

In his criticisms of Exhibit "B" attached to Mr. Manschreck's affidavit (NP Rec. 241) Mr. Peterson insists that the total reduction on Mr. Manschreck's theory should be $31,552.81 instead of $37,525.65 as shown in Mr. Manschreck's exhibit. In our final calculations we will therefore use the figure of $31,552.81 instead of the figure found by Mr. Manschreck.

ASSIGNMENTS NP-19 TO NP-21*

COURT'S ERROR IN FINDING THAT OPERATING EXPENSES INCIDENT TO MAINTENANCE OF WAY AND STRUCTURES AND FREIGHT-TRAIN CAR REPAIRS SHOULD BE DETERMINED BY THREE-YEAR INSTEAD OF ONE-YEAR AVERAGE.

With the above exceptions the operating expenses and revenues for the single year, 1933, were taken by the N. P. as the test in making its calculations. But as to maintenance of way and structures and freight-train car repairs, the annual average for 1931 to 1933 was taken. It would seem that if the results of more than one year's operations were taken as to these large items of expense, the same period should be used as to all other items of expense and revenues. There was no showing as to the amount of deferred maintenance of way and structures and equipment there may have been at the beginning of this three-year period taken as the test. The amount of freight-train car repairs expense necessary for a given period would, of course, depend upon the condition of the cars at the beginning of the period, as well as the extent of the use of the cars during such period. Mr.

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*(NP 19) The court erred in finding that the N. P.'s operating expenses incident to maintenance of way and structures should be determined by taking the annual average for three years instead of for 1933 alone, or that the N. P. had any deferred maintenance in 1933. (Finding XIII, NP Rec. 45.)

(NP 20) The court erred in finding that the N. P.'s total intrastate freight operating expenses classified as "Maintenance of Way and Structures," for the week of October 22, 1933, was $11,202.01, or was any sum in excess of $8,724.02 as shown by plaintiff's Exhibit "31." (Finding IX-e, NP Rec. 39, 217.)

(NP 21) The court erred in finding that the N. P.'s total intrastate freight operating expenses classified as "Freight car repairs, depreciation and retirement," for the week of October 22, 1933, was $9,552.01, or was any sum in excess of $8,372.41, as shown by plaintiff's Exhibit "32." (Finding IX-e, NP Rec. 39, 218.)

Peterson, who sponsored the three-year test, had no personal knowledge as to extent of such deferred maintenance if any. (NP Rec. 127, 210.)

Whatever may be said in justification of using a three-year instead of a one-year average as to these items, the fact remains that had only a one-year period been taken, the expenses for the year chargeable to intrastate freight traffic would have been $167,563 less than the amount charged in the N. P. Exhibit as shown by Manschreck's figures. (See item "M," Plff's Ex. "36," NP Rec. 220.) And see Manschreck's testimony in explanation of this and companion exhibits. (NP Rec. 188-192.)

ASSIGNMENT NP-22*

COURT'S ERROR IN FINDING THAT ANY SUM LESS THAN $1,127,464 SHOULD BE ASSIGNED AS NET JOINT FACILITY RENTS TO THE N. P.'s INTRASTATE OPERATIONS FOR 1933.

The N. P. pays out a certain amount each year for the use of the tracks and other facilities of other roads, and also receives from other roads certain rentals for the joint use of its own tracks and other operating property. The excess of the rentals so received over those paid out as to its Washington properties was, in the year 1933, $1,355,064 (NP Ex. "7," p. 8; NP Rec. 161.) Of this amount, the sum of $227,600.74 (NP Ab. 178) should be deducted as the net amount of the taxes

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*(NP 22) The court erred in finding that only $582,774, or any other sum less than $1,355,064, of the net joint facility rents received by the N. P. from its Washington operating properties should be assigned to the N. P.'s intrastate operations for 1933. (Finding XIV-b, NP Rec. 46-7.)

paid by foreign lines, which taxes seem to be credited as part of the joint facility rentals. This leaves, then, $1,355,064 less $227,600, or $1,127,464 as the net amount earned by the N. P. during 1933 as rental for the joint use of its facilities in Washington by foreign lines.

It is at once apparent that since this amount represents rentals of property located in Washington, and since such property, to the extent used by other lines, is not used by the N. P. in its interstate operations, the entire amount should be credited to the N. P.'s local operations.

As will later be shown, the G. N. insists that the excess of the joint facility rentals which it pays over those which it receives, should be treated as an operating expense item in determining whether it is making or losing money on its intrastate business. (See GN Ex. "11," pp. 1 and "A," GN Rec. 254, 258.) If this be true, then clearly the net amount received as such rentals should be added to the N. P.'s income in calculations made for the same purpose. In our discussion of the evidence in the G. N. case we will later point out (Post, pp. 165-171). why it is thought that neither joint facility rental paid nor joint facility rentals received should be considered in making these calculations. We are, however, submitting the net figures as shown in the N. P. case for use by the court should it conclude that such rentals received should be deemed a proper item of revenues, and the rentals paid be deemed a proper operating expense item.

ASSIGNMENTS NP-23 TO NP-26*

COURT'S ERROR IN COMPUTING N. P.'s GROSS REVENUES, OPERATING EXPENSES, TAXES, JOINT FACILITY RENTS, AND NET INCOME FROM ITS INTRASTATE OPERATIONS.

Duplication of Operating Expenses.—In the preparation of the N. P.'s Exhibit (N. P. Ex. "7") the N. P.'s witness, Peterson, assumed that all of the expenses charged to intrastate freight operations ($3,291,785; see N. P. Ex. "7," p. 6; NP Rec. 160) were expended solely in connection with the revenues credited under account 101, "freight," and that additional operating expenses should be charged in connection with all the other freight revenue credits. These additional freight revenue credits (other than account 110 "Switching") were as follows (Pltf.'s Ex. "25," NP Rec. 212A):

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*(NP 23) The court erred in finding that the N. P.'s total intrastate freight operating expenses for the week of October 22, 1933, was $75,078.42 or any sum in excess of $69,163.64 (Finding IX-e, NP Rec. 39); that the N. P.'s cost per revenue net ton mile was .98411c or any greater sum than $69,163.64 divided by 7,629,079 or .906579c, or that the N. P.'s total intrastate freight operating expenses for 1933 were $3,291,785 or any other sum greater than 334,493,591 multiplied by .906579c, or $3,032,448.64. (Finding IX-f, NP Rec. 39-40.)

(NP 24) The court erred in finding that the N. P.'s total intrastate operating expenses for 1933, other than taxes, were $4,796,440, or any other sum greater than $999,381 plus .6064 times the amount of the N. P.'s intrastate freight revenue for 1933. (Finding XII, NP Rec. 43-4.)

(NP 25) The court erred in finding that the N. P.'s total intrastate operating revenues for 1933 were only $5,271,893, or $5,493,252, or any other sum less than $5,802,530, as reported under oath by the N. P. to the D. P. W. for that year, and as alleged in its answer. (Findings X and XII, NP Rec. 42-4; Answer, NP Rec. 9.)

(NP 26) The court erred in finding that the N. P.'s net earnings from intrastate business for 1933 was a deficit of $228,623.22 or any other amount less than $817,443 if joint facility rents are not included, or $1,944,907 if joint facility rents are included. (Finding XII, NP Rec. 44.)

Acct. 111	Special service train	$1,149
112	Other freight train	102,002*
132	Hotel and restaurant	7,831*
135	Storage—freight	825
137	Demurrage	9,741
142	Rent of buildings and other property	5,569
143	Miscellaneous	46,504
151, 152	Joint facility—net debit	9,417 (red)
	Total	$164,204

The N. P. attempts to calculate these assumed additional operating expenses by first finding the ratio between the total operating expenses incident to intrastate freight service ($3,291,785) to the operating revenues received from intrastate freight operations credited to account 101, "freight" only, *i. e.*, $4,836,839, and then applies this percentage (68.06%) to the above sum, $164,204, thereby reaching a figure of $111,757, which it charges as additional operating expenses to intrastate freight operations. (See first calculation, NP Rec. 160.) But, as is conclusively shown by the affidavit of Mr. Manscheck (NP Rec. 232-241), in arriving at the figure of $3,291,785, the N. P.'s witness has already taken into account every item of operating expense incident to its entire intrastate freight operations with the exception of the starred items: "Other freight train, $102,002" (which we now concede, but is not shown in the Manschreck affidavit) and "Hotel and restaurant, $7,831." Excluding these starred items, the above total would be: $164,204 less $102,002 and less $7,831, leaving $54,371. Applying the operating ratio of 68.06% to this item, we have .6806 times $54,371, or $37,005 which constitutes a clear duplication of operating expenses in the N. P.'s Exhibit and should hence be deducted therefrom.

Mr. Manschreck, in his affidavit, most convincingly explains in detail this attempted duplication of expense, and to this affidavit we respectfully refer the court for further details as to our position. (NP Rec. 232-241.)

Conclusions as to N. P.'s intrastate income for 1933:

The results of the State's showing with respect to the items of expense discussed under the foregoing assignments may be summarized as follows:

N. P.'s railway operating income from 1933 intrastate operations as shown by N. P.'s calculations (N. P. Ex. "7," p. 1, NP Rec. 158)	$413,866 (red)
Plus excess charge for intrastate passenger operating expenses as shown by Manschreck (Plff's Ex. "26;" NP Rec. 213)—$1,500,957 (NP Ex. "7," p. 11, see footnote *ante*, pp. 105-6) less $999,381 (Plff's Ex. "26.") (See *ante*, pp. 108-111)	501,576
Such Ry. operating income after above correction..	$87,710
Plus excess charge for taxes apportionable to 1933 intrastate operations as shown by corrected showing made by Manschreck—$889,319 (NP Ex. "7," p. 7, NP Rec. 161) less $735,389 (Plff's Ex. "29," NP Rec. 215-6) less $43,491 (see *ante*, pp. 119-124)	$197,421
Such Ry. operating income after above corrections.	$285,131
Plus items of expense duplicated in N. P.'s calculations (see *ante*, pp. 138-9)	37,005
Such Ry. operating income after above corrections.	$322,136
Plus item of expense charged to intrastate operations as "pensions" (Plff's Ex. "37," NP Rec. 221; *ante*, pp. 125-7)	$103,471
Such Ry. operating income after above corrections	$425,607
Plus reduction in operating expenses charged to "Traffic expense," by apportionment on revenue instead of tonnage basis (Manschreck's Ex. "B," NP Rec. 241; *ante*, pp. 133-4)	$31,553
Such Ry. operating income after above corrections.	$457,160

Plus net amount by which N. P.'s railway operating income erroneously reduced by transferring revenues reported as intrastate, to interstate (*ante*, pp. 127-131), $169,485 less proportionate taxes: $43,491 (*ante*, p. 124)	$125,994
Such Ry. operating income after above corrections.	$583,154
Plus reduction in operating expense as to maintenance of way and structures and freight-train car repairs, if reported 1933 expense be taken instead of 3-year average (Item "M," Plff's Ex. "36," NP Rec. 220; *ante*, pp. 135-6)	$167,563
Such Ry. operating income after above corrections.	$750,717
N. P.'s railway operating income from 1933 intrastate operations after above corrections (Continued)	$750,717
Plus net joint facility rents received by N. P. on its Washington operating properties in 1933 (*ante*, pp. 136-7)	$1,127,464
N. P.'s net railway operating income from its 1933 intrastate operations after above corrections.	$1,878,181

EVIDENCE UNDISPUTED THAT N. P.'S NET EARNINGS WERE AT LEAST $729,940 FROM ITS INTRASTATE FREIGHT TRAFFIC IN 1933:

The N. P.'s various set-ups show its revenues and expenses incident to its intrastate passenger service separately from its revenues and expenses incident to its intrastate freight service. Consequently the results of its freight service operations alone may be readily calculated by deducting the revenues and expenses incident to its intrastate passenger service from its figures purporting to show the results of its combined intrastate freight and passenger service for that year.

The claimed "Result of Intrastate Operations" for 1933, freight and passenger, are set forth in NP's Exhibit "7", page 1 (NP Rec. 158) wherein the following results are shown:

(1) Gross operating revenues	$5,271,893
(2) Operating expenses	4,796,440
(3) Net revenue from railway operation	$475,453
(4) Railway taxes (on operating property)	889,319
(5) Railway operating income (deficit)	$413,866 (R)

Now, using this same form of set-up, and showing the corresponding figures incident to freight service alone, we have:

(1) Gross operating revenues	$5,271,893	
Less revenues from all intrastate passenger operations (Col. 2, Piff's Ex. "25", NP Rec. 212a; NP Ex. "7", p. 7, NP Rec. 161):	429,635	$4,842,258
(2) Operating expenses	$4,796,440	
Less operating expenses incident to intrastate passenger service operations (NP Ex. "7", p. 6, ln. 2, NP Rec. 160):	1,500,957	3,295,483
(3) Net revenue from freight service operations only (ln. 1 less ln. 2)		$1,546,775
(4) Railway taxes on operating property incident to passenger service only (NP Ex. "7", p. 7, NP Rec. 161)		816,835
(5) Railway operating income from freight service operations only (ln. 3 less ln. 4)		$729,940

NET LOSS CLAIMED BY N. P. ON 1933 INTRASTATE PASSENGER BUSINESS.

Revenues from passenger service (Piff's Ex. "25," vertical Col. 2, NP Rec. 212a)		$429,635
Operating expenses from passenger service other than taxes (NP Ex."7", p. 6, 2nd item, NP Rec. 160)	$1,500,957	
Taxes apportioned to passenger service (NP Ex. "7", p. 7, next to last item, NP Rec. 161)	72,484	$1,573,441

Net loss claimed by N. P. on 1933 intrastate passenger service	$1,143,806
Ratio between total expense and total revenues	366%
Cost of each dollar of revenue received	$3.66

ASSIGNMENTS NP-27 AND NP-28*

COURT'S ERROR IN PERMITTING PETERSON TO TESTIFY THAT THE N. P.'s INTRASTATE OPERATING EXPENSES WERE $251,000 GREATER IN 1933 THAN SHOWN BY THE N. P.'s SPECIAL STUDY, AND IN FINDING THAT THE USE OF SUCH TEST WEEK RESULTED IN AN UNDERSTATEMENT OF SUCH EXPENSES OF SOME $300,000.

Paragraph 4 of the Peterson affidavit, referred in Assignment NP-17 (*ante*, pp. 131-3) is to the effect that the study for the week of October 22, 1933, showed a traffic movement "greatly in excess of the average for 1/52 of a year" and if proper adjustment were made for that situation, the operating expenses as to intrastate freight traffic would be increased by $251,000 over those stated in N. P. Exhibit "7," page 1. (NP Rec. 243.) The State moved to strike this paragraph of the affidavit because not based on any record evidence before the court, which motion was denied. (NP Rec. 249-250.) The court thereupon stated that it was understood that paragraph 4 would be considered only in connection with

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*(NP 27) The court erred in refusing to strike paragraph 4 of Peterson's affidavit (NP Rec. 243) to the effect that the N. P.'s intrastate operating expenses for 1933 were $251,000 greater than as shown by N. P.'s Exhibit "7," on the ground that the same was not based on any record evidence before the court. (NP Rec. 249-250.)

(NP 28) The court erred in finding that the N. P.'s use of the test week of October 22, 1933, to determine its intrastate operating expenses resulted in an understatement of such cost for 1933 of approximately $300,000, or any other sum. (Findings IX-b and IX-g, NP Rec. 37-8, 40.)

and in explanation of evidence already in the record. (NP Rec. 250.)

The court will find that the only data or figures in the record that could possibly afford a basis for Peterson's conclusions are the figures which he gave over the objections urged in Assignments NP-3 and NP-4 (*ante*, pp. 98-101) as to the relative revenue and traffic during the test week and the whole of 1933. This testimony was hearsay and not the best evidence and was clearly inadmissible. Hence we insist (1) that Peterson's conclusions as to the intrastate freight operating expenses being greater than the results shown by N. P. Exhibit "7," page 1 (NP Rec. 158) were inadmissible and should be disregarded; and (2) that the court erred in making a finding based on such testimony.

The data and computations, if any, by which Peterson reached his conclusions are nowhere set forth in the record. The only figures mentioned in the record were pure hearsay. The records themselves were neither produced nor offered in evidence, and witness who, it is claimed, took off this data, was not produced as a witness. (See Assignment NP-3, *ante*, pp. 98-9.) Surely a revenue measure should not be set aside on mere estimates of this character. The following is quoted from the *Minnesota Rate Cases*, 230 U. S. 352, 465-6:

"We are of opinion that on an issue of this character involving the constitutional validity of state action, general estimates of the sort here submitted, with respect to a subject so intricate and important, should not be accepted as adequate proof to sustain a finding of confiscation."

The finding, it will be observed, is in any event erroneous, in that the excess is found to be $300,000,

whereas Peterson estimated it to be only $251,000. (NP Rec. 243; Findings IX-b and IX-g, Rec. 37-8, 40.)

ASSIGNMENT NP-29*

COURT'S ERROR IN REFUSING TO STRIKE AVERMENT IN PETERSON'S AFFIDAVIT THAT OPERATING RATIO ON N. P.'s SHIPMENTS FOR EXPORT WAS LOWER THAN ON ITS INTRASTATE FREIGHT TRAFFIC.

In paragraph 3 of the Peterson affidavit above referred to, the court will find certain averments as to the relative traffic density and cost per net ton mile on N. P.'s main and branch lines, and the conclusion that consequently in N. P.'s Exhibit "7" there was an excessive deduction made from intrastate freight operating expense by reason of elimination of so-called foreign commerce. (NP Rec. 243.)

Peterson conceded that there was nothing in the record to substantiate the conclusions and facts set forth in this paragraph. (NP Rec. 250.) The court denied the State's motion to strike this paragraph because not supported by anything in the record. (NP Rec. 243.)

For the reasons urged under Assignment NP-28 we submit that this paragraph should have been stricken, and that the facts therein averred should be disregarded.

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*(NP 29) The court erred in refusing to strike paragraph 3 of Peterson's affidavit (NP Rec. 243) to the effect that the N. P.'s operating ratio on shipments for export was lower than on its intrastate freight traffic. (NP Rec. 250.)

ASSIGNMENTS NP-30 AND GN-17*

COURT'S ERROR IN FINDING THAT IN PROPORTION TO REVENUE, COST OF THE N. P.'s AND G. N.'s INTRASTATE BUSINESS WAS GREATER THAN THE COST OF THEIR INTERSTATE BUSINESS.

This is truly a most remarkable finding in the light of the undisputed evidence. By operating ratio is meant the relation between operating expenses and operating revenues. The N. P.'s statistician found the N. P.'s operating ratio for *intrastate* freight traffic for 1933 to be 68.06% (NP Rec. 160), while Mr. Manschreck, the State's witness, found it to be 64.74% (NP Rec. 220, line "G"). Mr. Manschreck found the N. P.'s operating ratio for *interstate* freight traffic for 1933 (based on the N. P.'s own calculations) to be *91.20%* (NP Rec. 219, Line "E").

As to the N. P., no operating ratio as to either intrastate or interstate passenger traffic was computed by any witness, so that the court's finding is directly contrary to the undisputed facts.

In the G. N. case we again find the court reaching a conclusion directly contrary to the undisputed evidence. The G. N.'s statistician found the G. N.'s operating ratio for intrastate freight traffic for 1933 to be 51.33%. (GN Rec. 256, lines 1-b.) The operating ratio as to interstate freight traffic was not computed by any witness, but since it is the relation of operating expenses

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*(NP 30) The court erred in finding that, in proportion to revenue, the cost of the N. P.'s intrastate business is greater than the cost of such company's interstate business. (Finding IX-a, NP Rec. 37.)

(GN 17) The court erred in finding that in proportion to revenue, the G. N.'s cost per unit of doing intrastate business is greater than its cost per unit of doing interstate business. (Finding V, GN Rec. 60.)

to operating revenues, it is exceedingly easy to calculate. Thus:

(A) Total freight service operating revenues for 1933, interstate and intrastate (G. N.'s Ex. "11," p. 11, GN Rec. 268a)	$6,574,087
(B) Less freight service operating revenues for 1933, intrastate, as claimed by G. N. (G. N.'s Ex. "11," p. "B," GN Rec. 255)	1,622,644
(C) Total freight service operating revenues for 1933, *interstate* (A—B)	$4,951,443
(D) Total freight service operating expenses for 1933, interstate and intrastate (Piff's Ex. "25," line 2, GN Rec. 233)	$4,620,998
(E) Less total intrastate freight service operating expenses for 1933 as claimed by G. N. (GN's Ex. "11," p. "C," GN Rec. 256, line 1-c)	832,903
(F) Total freight service operating expenses, *interstate* (D—E)	$3,788,095
(G) Interstate freight service operating ratio (F ÷ C)	76.5%
Interstate freight service operating ratio (shown above)	51.33%

It is noted that in the G. N.'s calculations as to intrastate freight operating expenses a three-year average was taken as to maintenance of way and structures and freight train car repairs. This was a larger expense figure in each case than the figure for 1933 alone. Consequently, had we used the three-year average expenses as to these items as to interstate, we would have had a larger figure for line "D," and for line "F," and consequently a higher operating ratio for interstate freight service in line "G."

The operating ratio as to intrastate passenger service was shown to be 161.09% (G. N.'s Ex. "11," p. "C," GN Rec. 256, line 2-c), and a different ratio was not claimed as to interstate passenger service. Thus, as in the N. P. case, the court's finding is directly contrary to the undisputed facts.

ASSIGNMENT NP-31*

ERROR OF THE COURT IN FINDING THAT THE N. P.'S NET REVENUES WOULD BE LESS IN 1934 THAN IN 1933.

The findings of fact were made on March 25, 1935, nearly three months after the close of the year 1934, and at a time when the results of the N. P.'s 1934 operations must have been known to counsel who prepared these findings. Yet we find counsel preparing for the court a deliberate misstatement of facts regarding the N. P.'s 1934 operations. In the annual reports of the N. P. and G. N. to the tax commission for the year 1934, at pages 24 and 25, we find the following operating statistics for the years 1932 to 1934:

SYSTEM (N. P.)

	1932	1933	1934
Railway operating revenues	$47,084,176	$47,578,676	$51,407,775
Railway operating expenses	41,433,179	38,993,492	41,550,814
Net revenues from railway operations	$5,650,997	$8,585,184	$9,856,961
Railway tax accruals	6,677,354	5,883,251	5,312,592
Uncollectible railway revenues	23,209	23,848	16,575
Railway operating income	$1,049,567 (deficit)	$2,678,086	$4,527,795
Net railway operating income*	$1,990,389	$5,975,973	$7,915,209

*After adding rentals from joint facilities and equipment.

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*(NP 31) The court erred in finding that the tendency in 1934 was towards a substantial decrease in the N. P.'s net revenues, that increased cost of operation would be still greater in 1935, and that there was nothing apparent at the time said findings were made to suggest an increase in the N. P.'s gross revenues, but that the facts known suggested a decreased net income for 1935. (Finding V, NP Rec. 34-5; Conclusion 7, NP Rec. 53.)

STATE OF WASHINGTON (N. P.)

	1932	1933	1934
Railway operating revenues	$12,845,326	$12,064,954	$13,368,674
Railway operating expenses	12,336,819	11,145,042	11,675,083
Net revenues from railway operation	$508,507	$919,912	$1,693,591
Railway tax accruals	$2,730,016	$1,882,093	$1,833,863

SYSTEM (G. N.)

	1932	1933	1934
Railway operating revenues	$55,549,246	$61,923,891	$70,752,877
Railway operating expenses	45,655,673	41,545,224	48,610,181
Net revenues from railway operation	$9,893,574	$20,378,667	$22,142,696
Railway tax accruals	$6,697,424	$6,660,944	$6,181,111
Uncollectible railway revenues	14,210	7,213	10,527
Railway operating income	$3,181,940	$13,710,510	$15,951,058
Net railway operating income	$1,290,551	$11,810,227	$14,101,650

STATE OF WASHINGTON (G. N.)

	1932	1933	1934
Railway operating revenues	$8,389,154	$8,114,350	$9,062,655
Railway operating expenses	7,682,590	7,102,133	7,955,682
Net revenues from railway operation	$706,564	$1,012,217	$1,106,973
Railway tax accruals	$1,569,162	$1,363,567	$1,247,239

These reports being made pursuant to law, it would seem that statistical data contained therein should be matters of which the court should take judicial notice, particularly in actions wherein the constitutionality of a tax is attacked on the ground of insufficient earnings.

As a matter of fact, the increase in gross and net for 1932 over the 1933 figures was sufficiently forecast by Mr. Peterson, who testified for the N. P. on direct examination:

"The total operating revenues of the system for the eight months of 1934 were $33,044,301, an increase of $3,311,859 over the same period of 1933. During the same period the total operating expenses were $27,270,562 for the eight months of 1934, or an increase of $1,175,203 over the corresponding eight months in 1933. * * * Any estimate made for the balance of the year would be wholly conjectural. I don't know that it will be better in 1934 than in 1933. I think it will be pretty much the same as 1933. That is only an estimate that I make in the light of what knowledge I now have." (NP Rec. 112.)

Mr. Peterson's figures were of value as tending to indicate the upward trend of the business of these roads in 1934. But it is apparent that as a prophet, he had no better qualifications than the rest of us. If counsel wished to attempt to portray the future, he should have produced the then known facts and allowed the court to draw its own conclusions.

We are indeed at a loss to understand how, in the light of either the figures given by Peterson or the above reports, counsel for the N. P. would have the temerity to propose findings inducing the court to find that "the tendency in the year 1934 is toward * * * decreased net revenues." (NP Rec. 34-5.)

May we note here that these studies were made in one of the worst years in the history of these two roads. Whatever their intrastate earnings in 1933, who can say that such showing is representative of future years? The occupational tax act was in force but five months in 1933. Need we point out that a similar study made in 1934

would have shown quite different results. As was said in *Postal Tel.-Cable Co. v. Richmond*, 249 U. S. 252, 258:

"But a careful examination of the record fails to convince us that it contains that clear and convincing evidence that the tax thus falls upon interstate commerce which is necessary to justify a finding that the ordinance is unconstitutional and void."

APPENDIX "B"

Challenge to Trial Court's Findings of Fact and Rulings on Admissibility of Evidence in G. N. Ry. Co. v. State, No. 573.

ASSIGNMENT GN-4*

COURT'S ERROR IN FINDING THAT THE MAKING OF ACCURATE REPORTS AS TO THE G. N.'S INTRASTATE REVENUES WAS NEVER A MATTER OF IMPORTANCE PRIOR TO OCCUPATIONAL TAX ACT.

It is at once apparent that if it were contemplated that such reports were to be used as evidence in local rate investigations, such accuracy was always a matter of importance.

Nor are we so sure that these carriers are in a position to urge that it is not a matter of importance that a report required by statute to be made under oath be accurately made, and it is at least rather startling to find the lower court reaching such a conclusion.

Moreover, ever since 1929 both the G. N. and N. P. have been required to pay a fee of 1/10th of 1% on their gross operating revenue. (Laws 1929, Ch. 107, pp. 209-210; R. R. S. Sec. 10417.) In the case of the N. P. this fee is alleged to have been $6,481.32 for 1932 and $5,700.53 in 1933. (NP Rec. 15, 85.) The N. P.'s intrastate revenues were $6,613,959 and $5,802,530, respectively, in those two years. The G. N. alleges that this fee was $3,338.97 for 1932 and $3,137.05 for 1933 (and its local revenues $3,338,973 for 1932 and $3,137,047 for

*(GN 4) The court erred in finding that the making of accurate reports to the D. P. W. of the G. N.'s intrastate revenues was never a matter of importance prior to the imposition of the Occupational Tax Act of 1933. (Finding VI, GN Rec. 60-61.)

1933. (GN Rec. 14.) From these allegations it is evident that the fee was deemed both by the D. P. W. and the carriers to have been imposed only on intrastate revenues. Confirming this conclusion, Mr. Peterson testified on behalf of the N. P.:

"In paying this 1/10th of 1% tax that I have testified to, that is computed on the amount of local business in the way I have just described. * * * The N. P. has been paying the 1/10th of 1% tax for the years since 1929." (NP Rec. 87.)

Where these carriers have each, since 1929 been paying a tax or fee measured by their reported intrastate revenues, how is it possible, we ask, to sustain a finding that prior to the enactment of the occupational tax act in 1933 there was no incentive for these carriers accurately to report under oath their intrastate revenues to the D. P. W.?

ASSIGNMENT GN-5

(GN 5) The court erred in finding that the G. N. has never accurately reported its intrastate revenues to the D. P. W. (Finding VI, GN Rec. 60.)

Under the next assignment, we will show that no competent evidence was received at the trial showing that the G. N.'s intrastate revenues were other than as reported to the D. P. W.

But how, we ask, can such a finding be thought to aid these carriers who both base their calculations on the revenues as reported to the D. P. W.?

If it be true as found, that the G. N.'s reports as to State revenues have never been "accurately made" (GN Rec. 60), then surely the G. N.'s whole contention that it is doing business at a loss must fail. If there was no in-

centive to make accurate reports how can either the State or the G. N. rely upon such reports as evidence in a law suit involving the constitutionality of a tax?

ASSIGNMENT GN-6*

ERROR IN ALLOWING TESTIMONY THAT REVENUES ENTERED IN BOOKS AND REPORTED AS INTRASTATE WERE IN FACT INTERSTATE, WITHOUT REQUIRING PRODUCTION OF RECORDS FROM WHICH TAKEN.

The G. N. introduced in evidence Exhibit "11" upon which it relied to support its contention that in 1933 it lost money on its intrastate business. Pages 1 to 27 of this exihibit were based on the division of revenues between interstate and local business as reported by the G. N. to the D. P. W. for 1933. (GN Rec. 137, 142.) The results of this study are shown on page 1 of Exhibit "11" (GN Rec. 135-6, 258), and show that according to the G. N.'s own calculations, its railway operating income for 1933, after payment of taxes, was $491,544, and its net railway operating income (after deduction of joint facility rents and equipment rents paid) was $202,458. (GN Rec. 258.) In other words, *if the G. N. correctly entered upon its books of account, and correctly reported to the D. P. W. its intrastate operating revenues, said appellant, by its own admissions, wholly failed to prove that in 1933 it lost money on its intrastate operations.*

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*(GN 6) The court erred in permitting various of the G. N.'s witnesses to testify over plaintiff's objection that the same was hearsay and not the best evidence, that certain railway operating revenues for 1933 entered in the G. N.'s books of account and reported under oath to the D. P. W. as revenues from intrastate business, were in fact revenues from interstate business, and in refusing to strike such testimony after the same was so received. (G. N. Rec. 175-9, 183-193.)

Mr. Burn, the G. N.'s statistician (GN Rec. 115) prepared these pages 1 to 27, of Exhibit "11" and brought the same out from St. Paul to Seattle about a week before the trial, and after showing his exhibit to the company's attorneys, prepared the remaining pages, "A" to "F," in which a large amount of revenue shown on the G. N.'s books of account and report to the Washington D. P. W. to be intrastate revenues, were switched over to the interstate side of the ledger. (GN Rec. 141-2.) This revised showing was made from Identification "20" (GN Rec. 202) which was given to Mr. Burn after reaching Seattle. (GN Rec. 142.)

The following is a comparison of the G. N.'s interstate and intrastate revenues for 1933 as shown on its books of account and report to the D. P. W., with those used by Mr. Burns in the preparation of that part of Exhibit "11" which it is claimed shows that as to Washington intrastate business the G. N. was operating in the red in 1933:

Acct. No.	Account	As shown by G. N.'s books of account and report to D. P. W. (G. N.'s Ex. "11", p. 11, GN Rec. 268A)	After attempted change in G. N.'s books without production of underlying data. (Fdg. 7(g), GN Rec. 67-8)
101	Freight	$2,599,331	$1,502,153
110	Switching	41,977	38,367
111	Special Service Train	14	14
112	Other freight train	434	434
135	Storage—Freight	2,010	2,010
137	Demurrage	1,016	1,016
138	Telegraph and Telephone	4,095	3,653
142	Rents of buildings and other property	52,205	46,570
143	Miscellaneous	52,621	28,427
152	Joint facility—net debit	0	0
	Total Freight	$2,753,703	$1,622,644

Total revenue which court found without the production of any basic data, should be transferred from intrastate as shown by G. N.'s books and reports, to interstate..... $1,131,059

As noted above, this transfer of revenues from intrastate to interstate was made by Mr. Burn in accordance with a written statement (GN's Ex. "20") handed to him after reaching Seattle (GN Rec. 142). This statement was offered and received in evidence as a convenient statement showing what had been eliminated and not to prove the fact that the items thereon were properly to be eliminated as intrastate traffic (GN Rec. 175), and is as follows (GN Rec. 202):

Revenues eliminated as applicable to interstate and foreign commerce as reported in amended answers to interrogatories:

Account		Total Applicable Aug. 1, 1933, to Dec. 31, 1933	Total Applicable To Year 1933
(101)	**Freight:**		
(a)	Consignments originating in Washington and specifically billed for export..... $92,580		
(b)	Consignments originating in Washington and billed to warehouses and elevators, practically all of which would be exported or transported by water and/or rail to other states..... 65,558		
(c)	All other imports billed to Washington stations from Washington ports 8,033		
(d)	The initial local state revenue collected for shipments into transit stations..... 308,896		
(e)	Absorbed switching 14,997		
(f)	Milling in transit adjustment on grain originating outside of Washington and the products reshipped to points in Washington..... 41,055		
		$531,119	$1,097,178

Account	Total Applicable Aug. 1, 1933, to Dec. 31, 1933	Total Applicable To Year 1933
(110) **Switching:**		
Switching revenue received on shipments pertaining to (c) and (d) under account 101	1,820	3,610
(143) **Miscellaneous:**		
Wharfage		25,000
Total	$532,939	$1,125,788

The court's basis for finding that all these items of revenues were properly transferred from intrastate to interstate is the testimony of certain witnesses who testified over objection that the same was hearsay and not the best evidence, that they had examined certain records under the G. N.'s control in the state of Washington.

Thus, as to item "a," account No. 101, the G. N.'s witness Brown, testified that he made up that item of $92,580, not from the original records, but as to apples and flour from punch cards in the general office showing shipments of flour and apples from Washington stations to the Seattle dock, and as to all other shipments, from answers to letters written to all stations and ports in Washington asking for statements of billing covering all carload shipments originating in Washington and destined to the Seattle dock. (GN Rec. 175-6.) The witness believed that copies of the way bills from which the data was originally taken were in the hands of the G. N.'s forwarding agents in Washington. (Ab. Rec. 181.) He testified further that the only way the State's attorney could possibly check his figures as to item "a," would be by an examination of those way bills. (GN Rec. 181.)

The G. N.'s witness, Berger, testified that the information regarding item "a" was obtained direct from

the defendant's records in its Seattle dock office, consisting of the expense bills, demurrage records and other accounts kept there. Only one month's records were checked. (GN Rec. 191-2.)

As to item "b" the information was obtained by letter from agents in Seattle, Tacoma, Everett and Bellingham. Witness Brown wrote to the agent and asked him, and the agent wrote back and purported to give him the information asked. (GN Rec. 177-8, 180-181.) This information was shown by the G. N.'s books in Seattle.

As to item "c," the information was taken from copies of way bills and bills of lading and was shown by the G. N.'s books in Seattle. (GN Rec. 192.)

As to item "d," Brown got his information from punch cards the same as in the case of item "a." (GN Rec. 182.) The original records consisting of the expense bills were available in Seattle, and were checked there by the G. N.'s witness, Berger. Only a month's business was so checked. (GN Rec. 192.)

Item "e" was a debit item, transferred from interstate to intrastate. (GN Rec. 182.) The underlying data upon which the same was based was not offered in evidence, and the State, without success, moved to strike the testimony regarding the same on the ground that the same was hearsay and not the best evidence. (GN Rec. 183, 193.)

The information as to item "f" was taken from reports furnished to the G. N.'s witness, Brown, by the Transcontinental Freight Bureau, an agency of all the carriers. The information was contained in way bills located in the State of Washington. (GN Rec. 183.) It

was also shown by the expense bills at Seattle from which Berger purported to make his check. (GN Rec. 193.)

The information as to Account 110, "Switching," was taken from a letter received by the G. N.'s witness, Tower, from the auditor of station accounts, which was his sole source of information. (GN Rec. 185-6.)

The information as to Account 143, "Wharfage," was shown in the station records at the G. N.'s Seattle dock. (GN Rec. 185.)

The record shows that not only was the testimony offered regarding all of these items objected to as hearsay and not the best evidence, but after the same was received appropriate motions to strike were made on the same grounds. (GN Rec. 175-193.)

We respectfully submit that all of this testimony should rightfully have been excluded under the "best evidence" rule. It must be remembered that this showing was made for the purpose of attempting to establish the falsity of the G. N.'s own records and 1933 sworn report. The company's own records would, of course, be the best evidence of what constituted its intrastate revenues. And surely, when it attempted to show that these records and its official report to the State regulatory body were untrue, it should, we submit, if the best evidence rule is ever to be applied, have been required to produce the original records showing these claimed errors. It goes without saying that the State's attorney and witnesses were wholly powerless either to cross-examine or to check the statements of these witnesses as to the justification for these attempted changes.

"It is a general demand of the law that the best possible evidence be produced, and secondary evidence is admissible only when it is clearly made to appear that primary evidence is, for some good and sufficient reason, unattainable, and then only after a showing of diligence."

Kennedy v. Canadian Pac. R. Co., 87 Wash. 134, 135;

Case Threshing Machine Co. v. Wiley, 89 Wash. 301, 303;

Seid Chee v. Sanitary Fish Co., 103 Wash. 345, 348.

"Where the controversy is over the contents of a written document, the document itself is, of course, the best evidence;"

Hoptowit v. Brown, 115 Wash. 661, 669-670.

We are, of course, not unmindful of the voluminous evidence rule which, under certain conditions, permits the introduction of the results of voluminous facts contained in writings. This rule is set forth in *Corpus Juris* as follows:

"Where the results of voluminous facts contained in writings, or of the examination of many books and papers or records are to be proved, and the necessary examination of this documentary evidence cannot be conveniently or satisfactorily made in court, it may be made by an expert accountant or other competent person and the results thereof may be proved by him, if the books, papers, or records themselves are properly in evidence, or their absence satisfactorily explained, the admission of such testimony being a matter resting largely in the discretion of the trial court. It seems, however, that the jury are not bound by the result thus ascertained, but may make their own calculations from the books and papers in evidence."

22 C. J. 1017.

We submit that the admission of this testimony without requiring the production of the books and rec-

ords from which the alleged facts were ascertained for use in cross-examination and making a counter-showing, was palpably unjust to the State in the present case. The G. N., as noted, had reported all of these items of revenue as intrastate in its 1933 report to the D. P. W. This report was made under oath. (Rem. Rev. Stat. Sec. 10416.) The details of this report were, of course, based upon the same way bills, bills of lading, and other writings as were those of the witnesses produced by the G. N. to impeach its own records. Surely, before allowing this company to impeach its own books of accounts and sworn report, it should have required that the company produce its records (all available in Washington) or properly authenticated copies thereof for examination by the court and opposing counsel.

ASSIGNMENT GN-7

(GN 7) The court erred in refusing to strike pages "A" to "F" of G. N.'s Exhibit "11," on the ground that the same was hearsay and based on records available but neither produced nor offered in evidence. (GN Rec. 228-9.)

As already pointed out, pages "A" to "F" were based upon testimony shown under the last assignment to have been clearly inadmissible. For the reasons there urged, we respectfully submit that the motion to strike should have been granted.

ASSIGNMENT GN-8*

COURT'S ERROR IN FINDING THAT THE G. N.'S 1933 INTRASTATE REVENUES WERE OTHER THAN REPORTED TO THE D. P. W.

As shown under Assignment GN-6, there was no competent evidence that the G. N's 1933 intrastate revenues were other than as reported to the D. P. W. Consequently there was no basis for the court's finding that such revenues were other than as so reported.

ASSIGNMENT GN-10

(GN 10) The court erred in finding that in the apportionment of operating revenues received from nterstate freight business to the G. N.'s Washington operating properties, such properties were not entitled to more than a mileage prorate of such interstate freight revenues. (Findings VII-e, GN Rec. 64-7.)

This question has already been fully considered in connection with Assignment NP-11, to which discussion the court is respectfully referred. (*Ante*, pp. 111-118.)

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*(GN 8) The court erred in finding with respect to the G. N.'s 1933 intrastate operating revenues,—

(GN 8-a) That the total thereof was only $2,179,760, or any sum less than $3,305,548 as reported under oath to the D. P. W. (GN Rec. 268-a);

(GN 8-b) That the amount of such revenues assignable to "Freight," Account 101, were only $1,502,153, or any sum less than $2,599,331;

(GN 8-c) That the amount of such revenues assignable to "Switching," Account 110, were only $38,367, or any sum less than $41,977;

(GN 8-d) That the amount of such freight revenues assignable to "Rents of Buildings and Other Property," Account 142, were only $46,570, or any sum less than $52,205; and

(GN 8-e) That the amount of such freight revenues assignable to "Miscellaneous" were only $28,427, or any sum less than $52,621;

All as shown by the G. N.'s books of account and sworn report to the D. P. W. for 1933. (Findings VI and VII-g, GN Rec. 60-1, 67-8, compared with G. N. Ex. "11," p. 11, GN Rec. 268a.)

ASSIGNMENTS GN-9 AND GN-11 TO GN-16*

COURT'S ERROR IN FINDING THAT G. N. CONDUCTED ITS 1933 INTRASTATE OPERATIONS AT A LOSS.

To support its contention that it lost money on its 1933 Washington intrastate business, the G. N. offered in evidence G. N. Exhibit "11." This exhibit, as heretofore noted, makes two showings as to the results of the G. N.'s 1933 intrastate operations. Pages 1 to 27 are prepared on the assumption that the company correctly entered on its books of account, and correctly reported to the D. P. W. its 1933 interstate and intrastate revenues. We will, for convenience, call this its "book

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*(GN 9) Having found that an amount of the G. N.'s traffic reported to the D. P. W. for 1933 as intrastate, was in fact interstate traffic to the extent that such 1933 intrastate operating revenues were in fact only $2,179,760 instead of $3,305,348, as reported under oath to said D. P. W., the court erred in finding with respect to G. N.'s intrastate operations for 1933,—

(GN 9-a) That its operating expenses were $1,730,361, or any sum in excess of $1,675,206 (Finding VI, GN Rec. 60-61);

(GN 9-b) That its net revenues from railway operations were only $449,399, or any sum less than $504,554 (Finding VI, GN Rec. 61);

(GN 9-c) That its railway tax accruals were $335,247, or any sum in excess of $211,532 (Findings VI and VII-e, GN Rec. 61, 64-7);

(GN 9-d) That its Joint Facility rent—net debit, was $193,455, or any sum greater than $140,800 (Finding VI, GN Rec. 61);

(GN 9-e) That its net railway operating income was a deficit of $99,269, or any sum less than $132,256. (Finding VI, GN Rec. 61.)

(GN 11) The court erred in finding that the 1933 ad valorem taxes paid on the G. N.'s Washington operating properties should be apportioned as between intrastate and interstate service on the basis of the relative revenues derived therefrom (with only a mileage prorate of interstate revenues apportioned to Washington), or on any basis other than the relative use made by the G. N. of its Washington operating properties as reflected by the only available factors shown by the record, to-wit: relative car and locomotive

showing." But pages "A" to "F" are prepared on the theory that the company's books and official reports were untrue, and that some $1,131,059 of the revenues shown therein as intrastate, were in fact interstate revenues. This we will refer to as the "revised showing." The results of these two sections of G. N. Exhibit "11" are summarized on pages "1" (GN Rec. 258) and "A" (GN Rec. 254) of the exhibit. Page "1" shows the results of the "book showing;" page "A," the results if the company's books and reports were incorrect, i. e., its "revised showing."

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miles (as between freight and passenger), and relative freight car miles as between intrastate and interstate freight service. (Finding VII-e, GN Rec. 64-7.)

(GN 12) The court erred in finding that the G. N.'s net debit of $794,018 for joint facility rents in Washington for 1933 were assignable to its intrastate business on the basis of relative operating expenses intrastate and interstate, or on any basis other than the G. N.'s relative use of such jointly used properties in its intra and interstate operations as reflected by the only available factors shown by the record, to-wit: relative car miles (as between freight and passenger), and relative net ton miles as between intrastate and interstate freight service. (Finding VII-d, GN Rec. 63-4.)

(GN 13) The court erred in finding that pensions paid were properly chargeable as part of the G. N.'s operating expenses for the purpose of determining its railway operating income for 1933. (Finding VII-j, GN Rec. 69.)

(GN 14) The court erred in finding that the G. N.'s operating expenses incident to maintenance of way and structures and freight car repairs should be determined by taking the annual average for three years instead of for 1933 alone. (Finding VII-i, GN Rec. 68-9.)

(GN 15) The court erred in finding that G. N.'s Exhibit "11" showed the results of the G. N.'s intrastate operations in Washington during 1933 with substantial accuracy. (Finding VII-k, GN Rec. 69.)

(GN 16) The court erred in finding that the G. N.'s intrastate business as a steam railway company was conducted at a loss during 1933. (Finding VIII, GN Rec. 69-70.)

Joint facility rents paid not deductible as an operating expense:

Before analyzing the G. N. computations, let us first consider whether it is the deficit or earnings status of the *property,* or the deficit or earnings status of the *operating company,* which is determinative of whether the occupational tax is a burden on interstate commerce. If the intrastate operations of the operated properties themselves (independent of the question of ownership) show a railway operating income sufficient to pay the occupational tax payable on such operations, can it be said that because the operating company is losing money, the occupational tax must be paid from interstate revenues and is consequently a burden on interstate commerce?

In other words, is the criterion the *earnings of the properties operated* or the *earnings of the operating company?*

It is our position that it is the results of the operations of the particular *properties* operated by the tax-paying company which is the test, and it is not material whether the operating *company* is in fact losing or making money as a result of such operations. In other words, in determining whether the occupational tax is a drain on interstate revenues, it must be assumed that the operating company is the absolute owner of all of the property and interests in property employed in its railway operations. Thus, if a company has the legal title to its operating property, but such property is heavily mortgaged, the interest payable on such mortgages is not to be treated as an operating expense. And if, instead of constructing its own road, a company elects to

rent operating rights over another road, the rentals paid can no more be deemed an operating expense than can the bond interest payments on the portion of its operating property as to which it chances to hold the legal title. The same is true as to the equipment used. It can have no greater right to deduct as an operating expense the rentals paid for the use of the equipment it uses, than it would have to deduct as an operating expense the interest on the equipment trust notes which may be a lien upon its own equipment.

The fact is that the joint facility rental paid is the practical equivalent of interest payments on bonds issued for the construction of the company's own road. Had the G. N. constructed its own line from Seattle to Portland, it would have issued bonds to finance the new construction and would have paid, we may fairly assume, 4% to 5% interest thereon. Instead, it is, under the joint user agreement, required to pay one-third of 4½% on the cost of the property including additions and betterments. Surely this rental can no more be deemed an operating expense than could the interest payments on the company's outstanding bonds.

Moreover, it was the N. P.'s contention that in determining whether that company was making or losing money on its intrastate business, the test figure was "Railway Operating Income" computed by deducting "operating expenses" and taxes paid from "Gross operating revenues." (See NP Ex. "7," p. 1; NP Rec. 158.) In other words, counsel for the N. P. contended that join facility rentals *received* were not to be considered as operating income. (NP Rec. 97-8.) If this be true, we must likewise insist that the joint facility rental *paid*

by the G. N. cannot be deemed an operating expense in determining whether that road is making or losing money on its intrastate business.

The test is, we submit, is the *property* making a profit on intrastate business sufficient to pay the occupational tax imposed? If so, the tax cannot be deemed a direct burden on interstate commerce, even though the operating *company,* because of fixed interest and rental charges, is not making a corporate profit.

The case of *Atlantic Coast Line v. Daughton,* 262 U. S. 413, is, we submit, in point. There the Income Tax Law of North Carolina directed that the "net operating income" of railroads within the State be determined upon the basis of accounts to be kept according to the methods established by the Interstate Commerce Commission, and laid a tax upon the "net income," to be ascertained by deducting from "net operating income" only uncollectible revenue, certain taxes, and amounts paid for car hire, thus treating the railroad property within the State as the thing of which the income is taxed, and taking no account of other income of the corporation owning the railroad and making no deduction of its capital charges such as rent paid for lease of road or joint user rights. It was held that the statute, considering this distinction, did not, in effect, depart from the I. C. C.'s definition of net income, nor, as applied to interstate railroads, did it directly burden interstate commerce.

The same is true of the occupational tax here under consideration. It is the business of operating the particular property which is taxable, and not the individual

or corporation chancing to conduct such operations. Section 2 (2), subdiv. (e), Ch. 191, Laws 1933, provides:

"Upon every person engaging or continuing within this state in the following businesses; as to such persons the amount of tax or excise shall be equal to the gross income of the business multiplied by the rate set out after the business, as follows:

* * * * * * * * *

"III. Steam railways: one and one-half percent;"

Thus, the tax is measured by the gross income from the operation of the steam railway property, not by the income of the corporation. Just as in the *Daughton* case, the railroad property within the State is the thing of which the income is taxed, and no account is taken of the other income of the corporation chancing to own or operate such property. The following is quoted from the *Daughton* case (262 U. S. 413, 416, *et seq.*):

"Whether the statute is unconstitutional because it fails to include among the deductions from income allowed public service corporations the capital charges, including other rentals paid, is the main question for decision.

* * * * * * * * *

"* * * The contentions are that the statute, in fact, taxes gross income; that the classification as made by it is unreasonable; and that for these, and other, reasons it violates both the federal and the state constitution. All the contentions are, in our opinion, unsound."

After pointing out that the net income is computed by deducting from operating revenues, the operating expenses, uncollectible revenue, taxes paid, and car hire, the court then shows it to be the contention of the contesting railroads that the State should have credited as revenues all of its other corporate income including income from lease of road and joint facility rent income, and charged against such revenues all of its corporate

expenses including rent paid for lease of road and rents paid for joint facilities. Answering this contention, the court continues (p. 419):

"Thus the State takes, as the entity to be taxed, the railroad property operated by the Seaboard within the State. Therefore, it takes, as the primary basis for the tax, only operating revenues; that is, the gross receipts from operating such property. The Seaboard, on the other hand, assumes, as the entity which should be taxed, the company in respect to its North Carolina interests. Therefore the Seaboard takes, as the primary basis for the tax, in addition to the operating revenues of the lines within the State, North Carolina's proportion of the non-operating income of the company derived from other property owned by it, wherever situated. For the Seaboard, like most other railroad systems, is, to some extent, a holding company, as well as an operating company; and, as holding company, receives dividends from other concerns, interest on bonds of other concerns, and rental from property owned but not operated. As the State treats the operated property as the entity, it does not concern itself with interest charges and the rentals paid, just as it does not concern itself with a mortgage upon the real estate when it lays the *ad valorem* tax. On the other hand, as the Seaboard treats the company—the person—as the entity to be taxed, it undertakes to ascertain the net income of the company. This includes as gross income, a proportion of the receipts from property not within the State and includes among the deductions from the gross income of the company, the capital charges.

"That a State may, consistently with the Federal Constitution, impose a tax upon the net income of property, as distinguished from the net income of him who owns or operates it, although the property is used in interstate commerce, was settled in *Shaffer v. Carter*, 252 U. S. 37, 44, 52. There an Oklahoma statute was sustained which laid the tax upon the net income of Oklahoma oil property owned by a citizen and resident of Illinois. * * * It is a common provision in state income tax laws to tax the net income of property within the State which is owned, or operated, by non-residents. The differences between the parties arise, in the main,

not from difference in the method of determining what is net income, but from difference as to what is the subject of the tax. In other words, they differ as to the thing of which the net income is to be ascertained. This will appear from an examination of the several grounds on which the validity of the statute is assailed.

"*First.* The contention that the statute is obnoxious to the commerce clause rests upon the argument that the State's definition of net income differs from that adopted by the Interstate Commerce Commission * * *. A conclusive answer to that argument is found in the fact that the State adopts (without modification) the commission's definition for the net income of that which it taxes. For treating as the entity to be taxed, the railroad property operated by the company within the State, it appears that every item which the railroad claims the statute wrongly disallowed as a deduction is of such a character, that it is either clearly a capital charge (as distinguished from an operating charge) or reasonably may be deemed such as a matter of accounting."

At this point, the Court continues in a note to which reference is made (p. 421):

"To prove that the statute, in fact, taxes some part of the gross earnings, attention is called specifically to some minor items which the statute does not allow as deductions. But these stand in no different position than the major items—interest on funded debt and leased line rentals—discussed above. Prominent among these lesser items is 'joint facility rents' which, in the case of the Seaboard, amounted net to $21,816.81. Joint facility rents paid were $34,480.98; those received (credited as non-operating income) were $12,664.17. This is rental paid for railroad facilities—like tracks, terminals and roundhouses. They are needed by the carrier as a part of the plant and, not being owned, are rented from others. The fact that they are used jointly with others, is, of course, immaterial. This rent, like the rent of a leased line, is paid to secure control of the property operated. Hire of freight cars might have been treated in the same way, but the State, for reasons satisfactory to it, permitted that financial charge to be deducted, and to that extent reduced the tax."

The occupational tax is imposed on the activity of operating the railroad operating property under the control of the G. N. and is measured solely by the intrastate revenues derived from such operation. Clearly, such tax cannot be a burden on the interstate business handled on this same property if the net income from these *properties'* intrastate activities is sufficient to pay the tax imposed.

We submit that the case cited is squarely in point.

IF JOINT FACILITIES RENTS NOT AN OPERATING CHARGE, THE G. N. IS ADMITTEDLY MAKING A SUBSTANTIAL PROFIT ON ITS INTRASTATE OPERATIONS.

In its "book showing" (G. N. Ex. "11," p. 1, line 5; GN Rec. 258) the "railway operating income" from the G. N.'s intrastate operations (after allowance for taxes) was shown to be $491,544. And even assuming the validity of its claim that a portion of the revenue reported and shown on its books as intrastate, was in fact, interstate revenue, its 1933 "railway operating income" from intrastate operations (after allowance for taxes) was $114,152 (G. N. Ex. "11," p. "A," line 5; GN Rec. 254).

Hence, even on its own showing, if joint facility rents are not a proper operating charge, the G. N. admittedly made a substantial profit on its intrastate operations even in so abnormal a year as 1933.

G. N. MADE A PROFIT ON ITS 1933 INTRASTATE BUSINESS THOUGH JOINT FACILITY RENT BE DEEMED AN OPERATING EXPENSE.

This is true, the State contends, because of fundamentally wrong theories followed in the G. N. calculations. Thus:

Duplication of operating expenses—The G. N. charged $79,239 as an operating expense under the head-

ing: "Operating expenses applicable to intrastate revenues (freight proportion) other than account 101 ($150,554 × 51.33%)." (G. N. Ex. "11," p. 7, line "C;" GN Rec. 265-6.) But it clearly appears from Manschreck's testimony (GN Rec. 203-4) that all of the G. N. operating expenses had already been charged in computing its "total freight operating expenses" amounting to $1,334,268 (G. N. Ex. "11," p. 7, line "B;" GN Rec. 265-6) except the item of $21,547 for "switching," (Plff's. Ex. "21," line "E;" GN Rec. 230) and that there was consequently an attempted duplication of expense in the G. N. figures amounting to $79,239 minus $21,547, or $57,692. This correction is on the "book showing" figures. On the "revised showing" (G. N. Ex. "11," pp. "A" to "F;" GN Rec. 254-7) the corresponding reduction would be: all items of intrastate freight revenue other than Acct. 101 "Freight," and Acct. 110 "Switching" (G. N. Ex. "11," p. "B"; GN Rec. 255), or $82,124 times 51.33% (the operating ratio applied by the G. N. See G. N. Ex. "11," p. "C," line "1-b"; GN Rec. 256) or $42,154.

Correction as to taxes—The state contends in the G. N. as in the N. P. case that taxes should be apportioned on the basis of the relative *extent* of use made of the G. N. properties in its intrastate and interstate operations. Thus, apportioning tax accruals on the same basis as we have more fully explained in the N. P. case (*ante*, pp. 123-4) we find that the taxes allocated to intrastate operations for 1933 (based on the G. N. "book showing") should have been $294,318 (Plff.'s Ex. "22," line "S;" GN Rec. 230-232) instead of $511,530 as contended for by the G. N. (G. N. Ex. "11," p. 9, line 5-f;

GN Rec. 267-8), or a reduction in expense of $511,530 minus $294,318 or $217,212. The corresponding reduction in the G. N.'s "revised showing," would be the difference between $211,532 (Plff.'s Ex. "27," line "I," GN Rec. 235-6) and $335,247 (G. N. Ex. "11," p. "C," line 4-c, GN Rec. 256), or a reduction of $123,715.

Correction as to joint facility rents—The G. N. attempts to apportion its net joint facility rentals paid, first as between freight and passenger (both intra and interstate) according to relative operating expenses, and then to apportion the total thus allocated as between intra and interstate according to relative gross revenues received in the two services. (G. N. Ex. "11," p. 9, GN Rec. 267.) The State contends on the contrary, that these rentals paid should be apportioned (if at all), as between freight and passenger (both intra and interstate) according to relative *extent* of use (*i. e.*, freight car miles as compared with passenger car miles), and that the intrastate freight proportion should be then determined according to relative net ton miles hauled in intra and interstate service, and that the intrastate passenger proportion (there being no other available factor) should be determined on a relative gross revenue basis. (Plff.'s Ex. "23," GN Rec. 232-3.) Following this method, the State reaches a total charge (based on the G. N. "book showing") of $193,027 (Plff.'s Ex. "23," line "M," GN Rec. 233) as compared with $257,427 contended for by the G. N. (G. N. Ex. "11," p. 9, sum of lines 4-g and 4-h, GN Rec. 267), or a reduction in this item of expense of $257,427 less $193,027 or $64,400. The corresponding reduction in the G. N.'s revised showing, would be the difference between $140,800 (Plff.'s Ex.

"28," line "G," GN Rec. 237-8) and $193,455 (G. N. Ex. "11," p. "E," GN Rec. 257) or $52,655.

Elimination of "pensions" as operating expense item—The propriety of charging "pensions" as an item of operating expense in a case of this kind, has been heretofore discussed in connection with the N. P. case. (*Ante,* pp. 125-7.) The evidence shows that if this item be eliminated the G. N.'s net railway operating income (according to its "book showing," G. N. Ex. "11," p. 1, GN Rec. 258) would be increased by $22,066. (Plff.'s Ex. "25," GN Rec. 233-4.)

If, on the other hand, the court finds it to be established by competent evidence that a certain amount of the G. N.'s revenues reported as intrastate, should be transferred to interstate, then its intrastate freight revenue for 1933 would be $1,622,644 (G. N. Ex. "11," p. "B," GN Rec. 255), instead of $2,753,703, as shown by its books and report to the D. P. W. (G. N. Ex. "11," p. 11, GN Rec. 268-a) and this item of $22,066, would have to be reduced to an amount represented by the proportion which $1,622,644 bears to $2,753,703, or 58.92%, making the amount 58.92% of $22,066, or $13,001.

Effect of above corrections—Summaries of the G. N.'s contentions are set forth on pages "1" and "A" of G. N. Exhibit "11." (GN Rec. 254, 258.) As already observed, the summary as to its "book showing" (G. N. Ex. "11," p. 1, line 9) shows that by its own calculations, taking the G. N. books and reports as to its division of intra and interstate earnings at their face value, its "Net Railway Operating Income" (after deducting joint facility rents and equipment rents in addition to taxes) on its Washington 1933 intrastate operations was

$202,458. Corrections as above indicated, however, give the following results:

Net Railway Operating Income as computed by defendant.	$202,458
Plus excess charge by reason of duplication of operating expenses as above indicated	57,692
Plus excess charge for taxes as above indicated	217,212
Plus amount improperly charged for "pensions" (*ante*, pp. —)	22,066
Plus excess charge for joint facility rents paid as above indicated	64,400
Total net railway operating income on G. N. Wash. 1933 intrastate operations as shown by plaintiff's correction of defendant's figures	$563,828

Except as to "pensions," this showing is summarized and the same result reached in a different manner by Mr. Manschreck. (Plff.'s Ex. "24," line 8; GN Rec. 233.)

The summary as to the G. N.'s "revised showing" (assuming certain of its revenues shown in its reports and on its books as intrastate, to be in fact interstate) shows the G. N. "Net Railway Operating Income" (after deducting joint facility rents and equipment rents in addition to taxes) on its Washington 1933 intrastate operations to be a deficit of $99,269. (G. N. Ex. "11" p. "A," line 9, GN Rec. 254.) Corrections as above indicated, however, yield the following results:

Net railway operating income as computed by G. N. on its "revised showing"	$99,269 (red)
Plus excess charge by reason of duplication of operating expenses as above indicated	42,154
Plus excess charge for taxes as above indicated	123,715
Plus excess charge for joint facility rents paid as above indicated	52,655

Plus amount improperly charged for pensions as above indicated	13,001
Total net railway operating income from G. N.'s Washington 1933 intrastate operations as shown by the state's correction of the G. N.'s figures	$132,256

Except as to "pensions," this showing is summarized and the same result reached in a different way by Mr. Manschreck. (Plff.'s Ex. "29," line 8, GN Rec. 238.)

From the foregoing it follows: (1) that if the G. N.'s books and reports are correct, the G. N. confessedly made a substantial profit on its intrastate operations; (2) that if joint facility rents are not deductible as an operating expense, the G. N. confessedly made a substantial profit on such operations, even if allowed to transfer to interstate, some $1,131,059 in revenues reported as intrastate; and (3) that even allowing such wholesale transfer of revenues, and allowing joint facility rents as an operating expense, the company still made $132,256 from such 1933 intrastate operations, were its intrastate expenses properly computed.

We respectfully submit, therefore, that neither the N. P. nor the G. N. has sustained its defense that it lost money on its 1933 intrastate operations and will consequently be compelled to pay its occupational tax out of interstate earnings.

EVIDENCE UNDISPUTED THAT G. N.'S NET EARNINGS WERE AT LEAST $430,184 FROM ITS INTRASTATE FREIGHT TRAFFIC IN 1933.

As in the case of the N. P., the G. N.'s set-ups show its revenues and expenses incident to its intrastate passenger service separately from its revenues and expenses incident to its intrastate freight service. Con-

sequently, the results of its freight service operations alone may be readily calculated.

The revised claimed results of the G. N.'s intrastate operations for 1933, freight and passenger, are set forth in GN's Ex. "11," p. "A" (GN Rec. 254) wherein the following results are shown:

(1) Gross operating revenues	$2,179,760
(2) Operating expenses	1,730,361
(3) Net revenue from railway operations	449,399
(4) Railway tax accruals	335,247
(5) Railway operating income	114,152
(6) Equipment rents—Net debit	19,966
(7) Joint facility rent—Net debit	193,455
(8) Total rentals—Net debit	213,421
(9) Net railway operating deficit (Item 5 less item 8)	99,269 (R)

Now, using this same form of set-up, and showing the corresponding figures incident to freight service alone, we have:

(1) Gross operating revenues from freight service only (GN Ex. "11", p. "B", Col. 2; GN Rec. 255):	$1,622,644
(2) Operating expenses incident to freight service only (GN Ex. "11", p. "C", GN Rec. 256, ln. 1-c)	832,903
(3) Net revenue from railway operations from freight service only (ln. 1 less ln. 2):	$789,741
(4) Railway tax accruals incident to freight service only (GN Ex. "11", p. "C", GN Rec. 256, ln. 4-c—15.38% of $1,622,644):	249,563
(5) Railway operating income from freight service only (ln. 3 less ln. 4):	540,178
(6) Equipment rents incident to freight service only (GN Ex. "11", p. "D", ln. 5-e, GN Rec. 256)—Net debit	16,825
(7) Joint facility rent incident to freight service only (GN Ex. "11", p. "E", ln. 7-e, GN Rec. 257)—Net debit	93,119

(8) Total rentals incident to freight service only (ln. 6 pluss ln. 7)—Net debit		109,944
(9) Net railway operating income incident to freight service only (ln. 5 less ln. 8)		$430,234

NET LOSS CLAIMED BY G. N. ON 1933 INTRASTATE PASSENGER BUSINESS.

Revenues from passenger service (GN Ex. "11", p. "B", 2nd vertical Col., GN Rec. 255)		$557,116
Operating expenses from passenger service other than taxes, car rentals and joint facility rentals (GN Ex. "11", p. "C", item 2-e, GN Rec. 256)	$897,458	
Passenger car rentals (GN Ex. "11", p. "D", item 5-j, GN Rec. 256)	3,141	
Joint facility rentals—Debit (GN Ex. "11", p. "E", item 7-j, GN Rec. 257)	100,336	
Taxes (15.38% of $557,116, See GN Ex. "11", p. "C", calculation line 4-c applied to passenger revenues; GN Rec. 256)	85,684	$1,086,619
Net loss claimed by G. N. on 1933 intrastate passenger service		$529,503
Ratio between total expense and total revenues		195%
Cost of each dollar of revenue received		$1.95

ASSIGNMENT GN-14

(GN 14) The court erred in finding that the G. N.'s operating expenses incident to maintenance of way and structure and freight car repairs should be determined by taking the annual average for three years instead of for 1933 alone. (Finding VII-i, GN Rec. 68-9.)

The propriety of using a three-year instead of a one-year average as the measure of operating expenses incident to maintenance of way and structures and freight train car repairs has already been considered in connection with Assignments NP-19 to NP-21, to which discussion the court is respectfully referred. (*Ante*, pp. 135-6.)

ASSIGNMENT GN-17

(GN 17) The court erred in finding that in proportion to revenue, the G. N.'s cost per unit of doing intrastate business is greater than its cost per unit of doing interstate business. (Finding V, GN Rec. 60.)

This assignment is covered by Assignment NP-30, to which reference is hereby made. (*Ante*, pp. 146-7.)

ASSIGNMENT GN-19

(GN 19) The court erred in finding that a substantial part of the G. N.'s investment in its railways in Washington was made by order of the Washington regulatory bodies. (Finding IX, GN Rec. 70.)

We are unable to find where this finding is substantiated by any evidence in the record. If such exists, the G. N.'s counsel will no doubt favor the court with the proper citations.

ASSIGNMENT GN-20

(GN 20) The court erred in permitting the G. N.'s witness, Burn, to testify over objection, as to the operating ratio in switching seven specified cars at different terminals. (GN Rec.158-9, 230.)

Mr. Burn, the G. N.'s witness, was permitted to testify over the objection of the State's counsel as to the switching cost, revenue and operating ratio in connection with the intra-terminal switching of seven different cars at different terminals of the G. N. (GN Rec. 158-9.) The State's objection and motion to strike were made on the following grounds:

"The ground that unless they are all put in, they are not material. That they might make a considerable revenue on one and no revenue on another. That defendant should not be allowed to detail a few instances

and not give them all. That if that is to be investigated, we will have to open up the whole subject of G. N.'s operating ratio as to switching service." (GN Rec. 158.)

We respectfully submit that the testimony was objectionable for the reasons set forth in the objection and motion to strike, and consequently should be wholly disregarded by this court.

APPENDIX "C"

Evidence Bearing on Appellants' Contention that Their Intra and Interstate Instrumentalities Are Inseparably Commingled.

It is, of course, unquestionably true that both the appellant telephone company and the appellant railroads use the same instrumentalities in carrying on their intra and interstate operations.

But it is equally certain that if either of these appellants proposed to renounce its intrastate business, the purchaser or purchasers thereof would continue to use such appellant's interstate instrumentalities in continuing such intrastate business, with the practical result that there would be no duplication of equipment or operating expense in carrying on the two activities.

Let us first consider the position of the appellant telephone company: As a practical proposition, it cannot, we submit, be assumed that on renouncing its local business, the P. T., less than 10% of whose business is interstate (*ante*, p. 74), would be entitled to interstate rates yielding a fair return on all of its present operating properties. True, the company showed that it uses 92½% of its present property in its intrastate telephone and telegraph service. (PT Rec. 40.) But this does not mean that on surrendering its local business it would be compelled to retain the *exclusive use* of such properties for its long-distance service. It is, of course, inconceivable, that the various communities of Washington are to go without exchange and intrastate long-distance telephone service because of the imposition of this 3% gross earnings tax.

"The Company supplies something the public wants. If by a catastrophe, or series of catastrophies, all that it has was either wiped out of existence or made altogether useless for its present purpose, the people of the state would be deprived of all telephone facilities. The demand that they should be replaced would be general and insistent. To meet it, a new plant would be required." *Chesapeake & Potomac Telephone Co. v. Whitman*, 3 Fed. (2d) 938, 941.

The people would demand and would receive local telephone service. But the P. T.'s renunciation of its local business would certainly not mean a duplication of service in the different communities which it now serves. It must be presumed that such company and any new organizations proposing to furnish the local service so renounced, would proceed like ordinary business men confronted by the same problem. Where local exchange telephone service is supplied by one company, a company furnishing long-distance but not local exchange service to the same community, does not duplicate the local plant, but makes proper joint user arrangements with the local exchange company whereby long-distance messages are sent and received through the local exchange. This is exactly what would happen should the P. T. elect to surrender its local business. It would dispose of that portion of its plant chiefly valuable for handling local business, reserving joint user rights for handling interstate long-distance telephone messages thereover. Consequently, no duplication of equipment or operating property would be required.

It was agreed that the telephone system in Ellensburg is owned by a company independent of the P. T. (PT Rec. 66). With respect to this and other similar independent properties, R. W. Mastick, this company's

chief witness, testified on cross-examination to the following effect:

The Pacific Company makes connections of long distance service between Ellensburg and Seattle. The making of connection between Ellensburg and Seattle differs none at all from the method of making connections between Olympia, where the company owns the plant, and Seattle. The character of the property utilized in the Ellensburg plant differs not at all from the plant in Olympia in making the connection, as far as the exchange plant is concerned. The Pacific Company owns the toll lines between the Ellensburg Company and Seattle. The Ellensburg Company owns the equipment in the toll offices in Ellensburg. It is proper to speak of Ellensburg as a "foreign exchange area" or an "independent exchange." There are 100 or 102 independent exchanges in Washington comparable with Ellensburg. He presumed that all of these 102 companies connect with the Pacific system. And the inter-exchange service, which is the toll service, is handled in exactly the same way between each of these 102 companies and exchanges belonging to the Pacific Company as between stations belonging to the Pacific Company. The P. T. doesn't have any plant and equipment in the independent exchanges. It operates it itself. The P. T. has no duplication of plant and equipment with any exchanges in the state of Washington belonging to another company. (PT Rec. 66-8.)

Where long distance telephone messages are transmitted from foreign exchanges to exchanges of the Pacific Company, the latter company has certain contractual relations with the company operating the

foreign exchanges. Foreign exchanges get 30% of whatever the Pacific Company is entitled to on originating business. If the message were received by the foreign exchange and originated on the Pacific line, the foreign line would not get anything at all. (PT Rec. 68-71.)

Referring to foreign exchanges as exchanges that are independent not only of the Pacific Company but of the Bell system there would undoubtedly be several thousand of such foreign exchanges in the whole United States. Asked whether, so far as he knew, the operations of the Pacific Company with any of these foreign exchanges located outside of Washington are or are not competitive, he replied that he didn't know of any competitive system on the Pacific Coast. Asked if the P. T. has any competitive system in territory served by the Bell system as far as long distance is concerned, he replied, not to his own knowledge; that he did not specifically know of any case as to any of these foreign exchanges, either within or outside the state of Washington where there is a duplication of service as between the Pacific Company or the Bell system and the independent companies. In each of those cases the arrangement for handling long distance messages as between the foreign exchanges and the Pacific Company is handled as a result of a contract entered into between the Pacific Company and the independent company. What he had said of the relation between the exchange at Ellensburg and the Pacific Company and the transmission of toll messages between Ellensburg and the Pacific Company would apply equally to the transmission of toll messages between the Pacific Company and any one of these foreign exchanges, either within or without

the state of Washington. If the Ellensburg company should sell out all of its operating property to the Pacific Company and the latter should thereafter continue to furnish to Ellensburg the same service, both local and long distance that it now enjoys, he didn't see that the Pacific Company would have to acquire any additional property in order to furnish such service. Should the Pacific Company conclude that it didn't care to operate the Olympia exchange any more as part of the Pacific Company's property, it would be perfectly possible for some independent company to buy the Olympia exchange properties, and to have the same operating agreements with the Pacific Company which the Ellensburg Company has. In that case, the two companies would not have to acquire any additional property in order to carry on the operation in the same manner the property is now being operated by the Pacific Company. That would be true of all local exchanges such as Olympia that are now being operated by the Pacific Company in the state of Washington. In other words, if the two companies were split, one operating the local exchange and one continuing to operate the balance of the system, you wouldn't have to acquire any more property and you wouldn't sell any more in order to continue to function with the same degree of efficiency. (Pt. Rec. 73-6.)

As to all long distance messages transmitted to and from stations in said foreign exchange areas and points reached by the Pacific Company's long distance service, the Pacific Company, by contract with such owning companies, utilizes the telephone equipment of such local companies in the transmission of such long distance messages to and from telephone stations in such foreign exchange areas for which said Pacific Company pays such

other company an agreed service charge or division of the long distance tolls. (PT Rec. 89.)

If the Pacific Company did elect to cease to perform intrastate local or long distance service, and elected thereafter to render only interstate long distance service, as it now performs, and if the company could secure a purchaser for its property principally used for its local service or intrastate service, it could, of course, sell and convey that property to another company, but it wouldn't be doing a solely interstate business that way, because the local exchange does an interstate business over those facilities. If the Pacific Company, having elected to handle only interstate service, did elect to sell its property to some other company, he supposed that by a contractual arrangement it could reserve the right to use that property by a joint user arrangement for its interstate service. And if if did, by a satisfactory arrangement, enter into that sort of contract with the purchasing company, it wouldn't be necessary, then, to duplicate the actual equipment of the two companies, to increase the amount of the equipment of the two companies in handling the two classes of service. And if, on the same hypotheses, it sold out one piece of property, say Olympia property, to one company and its Seattle property to another company, it could make the same joint user contracts with each of those companies. (PT Rec. 90-92.)

There are now in the United States a large number of telephone companies doing a long distance telephone business between thousands of local exchange areas in which the local telephone service is supplied by local telephone companies other than the company or com-

panies doing the long distance business. So far as he knew, in none of those areas does the long distance company handling the long distance messages, maintain separate equipment for long distance use only. But in such cases the long distance companies utilize by joint user agreements, the facilities of such local telephone companies in handling the long distance service. (PT Rec. 92-3.)

APPELLANT RAILROADS:

Obviously the intrastate operations of these roads are even more essential to the people of Washington than those of the appellant telephone company. And it would seem that either of these railroads would likewise, if it chose to dispose of its intrastate business to another company, enter into joint user arrangements with such purchaser, as a result of which the same facilities and employes would be used in carrying on both the intrastate and interstate operations. It is a common practice for two or more companies to use the same rails. Express and sleeping car companies use the facilities of a railroad, as does also the United States mail service. Why could not a separate and distinct company handling only intrastate business, by contract, use the same rails, trains, cars and employes as the company handling only interstate business?

In such case, of course, there would be no duplication of either operating expenses or of equipment.